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Supreme Court of the United States

OCTOBER TERM, 1937

No. 6

D. W. McEACHERN, ADMINISTRATOR OF THE ESTATE OF S. C. McEACHERN, DECEASED, PETITIONER,

vs.

J. T. ROSE, FORMER COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

PETITION FOR CERTIORARI FILED FEBRUARY 23, 1937.

CERTIORARI GRANTED APRIL 5, 1937.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1937

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[fol. a] [Caption omitted]

[fol. 1]

IN THE DISTRICT COURT OF THE UNITED STATES FOR THE NORTHERN DISTRICT OF GEORGIA, ATLANTA DIVISION

At Law. No. 1799

D. W. McEachern, Administrator of the Estate of S. C. McEachern, Deceased,

vs.

J. T. Rose, Former Collector of Internal Revenue

Petition—Filed September 11, 1934

To the District Court of the United States for the Northern District of Georgia, Atlanta Division:

The petition of D. W. McEachern, Administrator of the Estate of S. C. McEachern, deceased, Plaintiff, names J. T. Rose, former Collector of Internal Revenue as Defendant herein, and respectfully shows to this Honorable Court:

First Count

1

S. C. McEachern died, intestate, on December 12, 1928, a resident of Cobb County, Georgia. On February 4, 1929, the Ordinary of Cobb County, Georgia, granted letters tes-
[fol. 2] tamentary upon the Estate of said S. C. McEachern to D. W. McEachern, and on the same day said D. W. McEachern qualified as Administrator of the Estate of S. C. McEachern, deceased.

2

Defendant, J. T. Rose, is a citizen of the State of Georgia and is a resident and inhabitant of Fulton County in the Atlanta Division of the Northern District of Georgia, and during the period from December 5, 1921, to June 19, 1933, said Defendant was Collector of Internal Revenue of the United States for the District of Georgia, in which collection district the Plaintiff resides and the Estate of S. C. McEachern is being administered.

3

This is a suit of a civil nature arising under the internal revenue laws of the United States, and in particular the Revenue Act of 1928, being the Act of May 29, 1928, Chapter 852, 45 Stat. 795.

4

The Defendant is indebted to the Plaintiff in the principal sum of $230.07 with interest thereon at six per cent per annum from December 11, 1930, by reason of the facts set forth in the following paragraphs.

5

During the month of March, 1930, the Commissioner of Internal Revenue assessed against the Estate of S. C. McEachern income taxes for the calendar year 1929, in the sum of $924.96.

6

Defendant collected from Plaintiff the full amount of said assessment in the following installments, on the dates indicated:

[fol. 3] $231.01 on March 15, 1930.
231.94 on June 12, 1930.
231.94 on September 15, 1930.
230.07 on December 11, 1930.

7

The only items of gross income as defined in Section 22 of the Revenue Act of 1928 received by or on behalf of said Estate of S. C. McEachern in the year 1929 were (a) an item of rents received and (b) an item of gain derived upon the collection of certain installments of the selling price of stock in the Industrial Life & Health Insurance Company, both of which items will be more fully described below.

8

The item of rents referred to in the preceding paragraph amounted to $247.70.

9

The installments of the selling price of stock in Industrial Life & Health Insurance Company referred to in Paragraph

7 were received by the Estate of S. C. McEachern in the year 1929 in the sum of $26,250.00, pursuant to a contract for the sale of 500 shares of said stock, which the said S. C. McEachern, Plaintiff's intestate, had entered into on September 3, 1924. A copy of said contract is attached hereto and made a part hereof, marked Exhibit A.

10

Under said contract of sale (Exhibit A), the said S. C. McEachern undertook to sell said 500 shares of stock in Industrial Life & Health Insurance Company for a total consideration of $300,000.00, payable $30,000.00 in cash at the time of said contract and the balance in installments of $7,500.00, the first being due March 1, 1925, and the other installments being due every three months thereafter.

[fol. 4]

11

At the time of the death of said S. C. McEachern on December 11, 1928, there remained unpaid under said contract remaining installments in the total sum of $150,000.00, which was due as follows: Installments of $7,500.00 each due respectively on the first day of March 1929, and on the first day of each third month thereafter, the last payment being due December 1, 1933.

12

The unpaid and uncollected installment obligations in the sum of $150,000.00, as described in Paragraph 11, outstanding at the date of the death of S. C. McEachern, were treated as an asset of said S. C. McEachern for Federal estate tax purposes and were included under Schedule C of the Federal Estate tax return filed on behalf of the Estate of S. C. McEachern at a value of $125,000.00.

13

The value of $125,000.00, at which said S. C. McEachern's interest in said unpaid and uncollected installment obligations at the time of his death was returned for estate tax purposes, was determined by deducting from the face amount of the then future installment payments a discount of approximately 6.348 per cent per annum from the date of the death of S. C. McEachern to the average due date of the installments.

14

The only item of income or gain derived or received by the Estate of S. C. McEachern from the collection in 1929 of said installment obligations in the sum of $26,250.00 as described in Paragraph 9 above was the sum of $952,48, representing the discount of 6.348 per cent per annum on said collection for a period of seven and one-half months, [fol. 5] which was the average time elapsed from the date of the death of S. C. McEachern on December 12, 1928, to the dates of collection in 1929.

15

During the year 1929 interest was paid by and on behalf of the Estate of S. C. McEachern in the sum of $2,050.00, which sum represents a proper deduction under Section 23(b) of the Revenue Act of 1928.

16

During the year 1929 state, county and city taxes in the sum of $1,797.17 were paid by and on behalf of the Estate of S. C. McEachern, which sum represents a proper deduction under Section 23(c) of the Revenue Act of 1928.

17

The deductions properly allowable to said Estate of S. C. McEachern for the year 1929 exceeded the items of gross income as described above, and said Estate of S. C. McEachern had no net income subject to income tax for the year 1929.

18

On December 9, 1932, said D. W. McEachern as Administrator of, and on behalf of, said Estate of S. C. McEachern, filed with the Defendant a claim for refund on Treasury Department Form 843, requesting the refund of the amount here sued for and setting forth the facts and reasons upon which this suit is based. The Commissioner of Internal Revenue disallowed said claim for refund on a Schedule dated May 17, 1933, and Plaintiff was advised of said action by the Commissioner in accordance with the provisions of Section 3226 of the Revised Statutes, as amended, by notice sent by the Commissioner by registered mail on May 17, 1933.

[fol. 6] Wherefore, Plaintiff prays that process issue directed to the Defendant requiring him to be and appear at the next term of this Court to answer this petition, and Plaintiff further prays for judgment against the Defendant for the principal sum of $230.07, together with interest thereon at six per cent per annum from December 11, 1930, together with all costs of this proceeding.

Second Count

1

S. C. McEachern died, intestate, on December 12, 1928, a resident of Cobb County, Georgia. On February 4, 1929, the Ordinary of Cobb County, Georgia, granted letters testamentary upon the Estate of said S. C. McEachern to D. W. McEachern, and on the same day said D. W. McEachern qualified as Administrator of the Estate of S. C. McEachern, deceased.

2

Defendant, J. T. Rose, is a citizen of the State of Georgia and is a resident and inhabitant of Fulton County in the Atlanta Division of the Northern District of Georgia, and during the period from December 5, 1921, to June 19, 1933, said Defendant was Collector of Internal Revenue of the United States for the District of Georgia, in which collection district the Plaintiff resides and the Estate of S. C. McEachern is being administered.

3

This is a suit of a civil nature arising under the internal revenue laws of the United States, and in particular the Revenue Act of 1928, being the Act of May 29, 1928, Chapter 852, 45 Stat. 795.

[fol. 7]

4

The Defendant is indebted to the Plaintiff in the principal sum of $1,951.61, with interest at six per cent per annum on $434.62 from March 16, 1931, on $434.62 from June 11, 1931, on $434.62 from September 11, 1931, on $647.75 from December 15, 1931, by reason of the facts set forth in the following paragraphs.

5

During the month of March 1931, the Commissioner of Internal Revenue assessed against the Estate of S. C. McEachern income taxes for the calendar year 1930 in the sum of $1,951.61.

6

Defendant collected from Plaintiff the full amount of said assessment in the following installments, on the dates indicated:

$434.62 on March 16, 1931
434.62 on June 11, 1931
434.62 on September 11, 1931
647.75 on December 15, 1931

7

The only items of gross income as defined in Section 22 of the Revenue Act of 1928 received by or on behalf of said Estate of S. C. McEachern in the year 1930 were (a) an item of rents received and (b) an item of gain derived upon the collection of certain installments of the selling price of stock in the Industrial Life & Health Insurance Company, both of which items will be more fully described below.

8

The items of rents referred to in the preceding paragraph amounted to $995.06.

[fol. 8]

9

The installments of the selling price of stock in Industrial Life & Health Insurance Company referred to in Paragraph 7 were received by the Estate of S. C. McEachern in the year 1930 in the sum of $33,750.00, pursuant to a contract for the sale of 500 shares of said stock, which the said S. C. McEachern, Plaintiff's intestate, had entered into on September 3, 1924. A copy of said contract is attached hereto and made a part hereof, marked Exhibit A.

10

Under said contract of sale (Exhibit A), the said S. C. McEachern undertook to sell said 500 shares of stock in Industrial Life & Health Insurance Company for a total

consideration of $300,000.00, payable $30,000.00 in cash at the time of said contract and the balance in installments of $7,500.00, the first being due March 1, 1925, and the other installments being due every three months thereafter.

11

At the time of the death of said S. C. McEachern on December 11, 1928, there remained unpaid under said contract remaining installments in the total sum of $150,000.00, which was due as follows: Installments of $7,500.00 each due respectively on the first day of March, 1929, and on the first day of each third month thereafter, the last payment being due December 1, 1933.

12

The unpaid and uncollected installment obligations in the sum of $150,000.00, as described in Paragraph 11, outstanding at the date of the death of S. C. McEachern, were treated as an asset of said S. C. McEachern for Federal estate tax purposes and were included under Schedule C [fol. 9] of the Federal estate tax return filed on behalf of the Estate of S. C. McEachern at a value of $125,000.00.

13

The value of $125,000.00, at which said S. C. McEachern's interest in said unpaid and uncollected installment obligations at the time of his death was returned for estate tax purposes, was determined by deducting from the face amount of the then future installment payments a discount of approximately 6.348 per cent per annum from the date of the death of S. C. McEachern to the average due date of the installments.

14

The only item of income or gain derived or received by the Estate of S. C. McEachern from the collection in 1930 of said installment obligations in the sum of $33,750.00 as described in Paragraph 9 above was the sum of $3,333.32, representing the discount of 6.348 per cent per annum on said collection for a period of nineteen and one-half months, which was the average time elapsed from the date of the death of S. C. McEachern on December 12, 1928, to the dates of collection in 1930.

15

During the year 1930 interest was paid by and on behalf of the Estate of S. C. McEachern in the sum of $1,920.00, which sum represents a proper deduction under Section 23(b) of the Revenue Act of 1928.

16

During the year 1930 state, county and city taxes in the sum of $980.00 were paid by and on behalf of the Estate of S. C. McEachern, which sum represents a proper deduction under Section 23(c) of the Revenue Act of 1928.

[fol. 10] 17

During the year 1930 debts owing to said Estate of S. C. McEachern were ascertained to be worthless and charged off by the Plaintiff in the sum of $1,389.79, which sum consitutes a proper deduction under Section 23(j) of the Revenue Act of 1928.

18

The items of gross income received by said Estate of S. C. McEachern in the year 1930 exceeded the deductions properly allowable to said Estate by the sum of $38.59, which sum represents the net income of said Estate of S. C. McEachern for the year 1930 within the meaning of Section 21 of the Revenue Act of 1928. Said sum of $38.59 was offset by the exemption of $1,500.00 allowable to said Estate by Section 163 of the Revenue Act of 1928.

19

On December 9, 1932, said D. W. McEachern as Administrator of, and on behalf of, said Estate of S. C. McEachern, filed with the Defendant a claim for refund on Treasury Department Form 843, requesting the refund of the amount here sued for and setting forth facts and reasons upon which this suit is based. The Commissioner of Internal Revenue disallowed said claim for refund on a Schedule dated May 17, 1933, and Plaintiff was advised of said action by the Commissioner in accordance with the provisions of Section 3226 of the Revised Statutes, as amended, by notice sent by the Commissioner by registered mail on May 17, 1933.

Wherefore, Plaintiff prays that process issue directed to the Defendant requiring him to be and appear at the next term of this Court to answer this petition, and Plaintiff further prays for judgment against the Defendant for the principal sum of $1,951.61 with interest at six per cent per annum, as provided by law, on $434.62 from March 16, [fol. 11] 1931, on $434.62 from June 11, 1931, on $434.62 from September 11, 1931, and on $647.75 from December 15, 1931, together with all costs of this proceeding.

Third Count

1

S. C. McEachern died intestate on December 12, 1928, a resident of Cobb County, Georgia. On February 4, 1929, the Ordinary of Cobb County, Georgia, granted letters testamentary upon the Estate of said S. C. McEachern to D. W. McEachern, and on the same day said D. W. McEachern qualified as Administrator of the Estate of S. C. McEachern, deceased.

2

Defendant, J. T. Rose, is a citizen of the State of Georgia and is a resident and inhabitant of Fulton County in the Atlanta Division of the Northern District of Georgia, and during the period from December 5, 1921, to June 19, 1933, said Defendant was Collector of Internal Revenue of the United States for the District of Georgia, in which collection district the Plaintiff resides and the Estate of S. C. McEachern is being administered.

3

This is a suit of a civil nature arising under the internal revenue laws of the United States, and in particular the Revenue Act of 1928, being the Act of May 29, 1928, Chapter 852, 45 Stat. 795.

4

The Defendant is indebted to the Plaintiff in the principal sum of $1,676.66 with interest at six per cent per annum on $401.20 from March 15, 1932, on $416.65 from [fol. 12] June 17, 1932, on $416.65 from September 15, 1932, on $441.16 from May 31, 1933, and on $1.00 from June 8,

1933, by reason of the facts set forth in the following paragraphs.

5

During the month of March, 1932, the Commissioner of Internal Revenue assessed against the Estate of S. C. McEachern income taxes for the calendar year 1931 in the sum of $1,666.57.

6

Defendant collected from Plaintiff the full amount of said assessment in the following installments, on the dates indicated:

$416.65 on March 15, 1932
416.65 on June 17, 1932
416.65 on September 15, 1932
416.62 on May 31, 1933

7

On May 31, 1933, the Defendant collected from Plaintiff interest in the sum of $24.54 on the last installment of principal referred to in Paragraph 6, namely, the installment of $416.62 collected on May 31, 1933.

8

On June 8, 1933, the Defendant collected from Plaintiff interest in the sum of $1.00 on the last installment of principal referred to in Paragraph 6, namely, the installment of $416.62 collected on May 31, 1933.

9

The only items of gross income as defined in Section 22 of the Revenue Act of 1928 received by or on behalf of said Estate of S. C. McEachern in the year 1931 were (a) an [fol. 13] item of rents received and (b) an item of gain derived upon the collection of certain installments of the selling price of stock in the Industrial Life & Health Insurance Company, both of which items will be more fully described below.

10

The item of rents referred to in the preceding paragraph amounted to $248.54.

11

The installments of the selling price of stock in Industrial Life & Health Insurance Company referred to in Paragraph 9 were received by the Estate of S. C. McEachern in the year 1931 in the sum of $30,000.00, pursuant to a contract for the sale of 500 shares of said stock, which the said S. C. McEachern, Plaintiff's intestate, had entered into on September 3, 1924. A copy of said contract is attached hereto and made a part hereof, marked Exhibit A.

12

Under said contract of sale (Exhibit A), the said S. C. McEachern undertook to sell 500 shares of stock in Industrial Life & Health Insurance Company for a total consideration of $300,000.00, payable $30,000.00 in cash at the time of said contract and the balance in installments of $7,500.00, the first being due March 1, 1925, and the other installments being due three months thereafter.

13

At the time of the death of said S. C. McEachern on December 11, 1928, there remained unpaid under said contract remaining installments in the total sum of $150,000.00, which was due as follows: Installments of $7,500.00 each due respectively on the first day of March 1929, and on the [fol. 14] first day of each third month thereafter, the last payment being due December 1, 1933.

14

The unpaid and uncollected installment obligations in the sum of $150,000.00, as described in Paragraph 13, outstanding at the date of the death of S. C. McEachern, were treated as an asset of said S. C. McEachern for Federal estate tax purposes and were included under Schedule C of the Federal estate tax return filed on behalf of the Estate of S. C. McEachern at a value of $125,000.00.

15

The value of $125,000.00, at which said S. C. McEachern's interest in said unpaid and uncollected installment obligations at the time of his death was returned for estate tax purposes, was determined by deducting from the face

amount of the then future installment payments a discount of approximately 6.348 per cent per annum from the date of the death of S. C. McEachern to the average due date of the installments.

16

The only item of income or gain derived or received by the Estate of S. C. McEachern from the collection in 1931 of said installment obligations in the sum of $30,000.00 as described in Paragraph 11 above was the sum of $4,999.95, representing the discount of 6.348 per cent per annum on said collection for a period of thirty-one and one-half months, which was the average time elapsed from the date of the death of S. C. McEachern on December 12, 1928, to the dates of collection in 1931.

17

During the year 1931 interest was paid by and on behalf of the Estate of S. C. McEachern in the sum of $1,220.00, [fol. 15] which sum represents a proper deduction under Section 23(b) of the Revenue Act of 1928.

18

During the year 1931, state, county and city taxes in the sum of $898.71 were paid by and on behalf of the Estate of S. C. McEachern, which sum represents a proper deduction under Section 23(c) of the Revenue Act of 1928.

19

During the year 1931 said Estate of S. C. McEachern suffered and sustained a loss of property to the extent of $100.00, arising from the burglary of a store belonging to said Estate, which said loss was not compensated for by insurance or otherwise, and which said amount constitutes a proper deduction under Section 23(e) of the Revenue Act of 1928.

20

The items of gross income received by said Estate of S. C. McEachern in the year 1931 exceeded the deductions properly allowable to said Estate by the sum of $2,529.79, which sum represents the net income of said Estate of S. C. McEachern for the year 1931 within the meaning of Section 21 of the Revenue Act of 1928. Said sum of $2,529.79 was

subject to the exemption of $1,500.00 allowed by Section 163 of the Revenue Act of 1928 for normal tax purposes, and the remaining $1,029.79 was subject to normal tax at the rate of one and one-half per cent, or a total normal tax of $15.45.

21

On December 9, 1932, said D. W. McEachern as Administrator of, and on behalf of, said Estate of S. C. McEachern, filed with the Defendant a claim for refund on Treasury [fol. 16] Department Form 843, requesting the refund of the amount here sued for and setting forth the facts and reasons upon which this suit is based. The Commissioner of Internal Revenue disallowed said claim for refund on a Schedule dated May 17, 1933, and Plaintiff was advised of said action by the Commissioner in accordance with the provisions of Section 3226 of the Revised Statutes, as amended, by notice sent by the Commissioner by registered mail on May 17, 1933.

Wherefore, Plaintiff prays that process issue directed to the Defendant requiring him to be and appear at the next term of this Court to answer this petition, and Plaintiff further prays for judgment against the Defendant for the principal sum of $1,676.66, together with interest at six per cent per annum on $401.20 from March 15, 1932, on $416.65 from June 17, 1932, on $416.65 from September 15, 1932, on $441.16 from May 31, 1933, and on $1.00 from June 8, 1933, together with all costs of this proceeding.

Blair & Gardner, Sutherland, Tuttle & Brennan, Attorneys for Plaintiff.

EXHIBIT "A" TO PETITION

GEORGIA,
Fulton County:

This Contract and Agreement, made and entered into on this the 3rd day of September, 1924, by and between J. N. McEachern, Sr., of the County of Fulton and State of Georgia, party of the first part, and S. C. McEachern, of the County of Cobb County and State of Georgia, party of the second part, Witnesseth:

1. That for value received, the party of the first part does hereby agree to pay to the party of the second part, his heirs

[fol. 17] and assigns, the sum of Three Hundred Thousand & No/100 ($300,000.00) Dollars; said sum payable as follows: Thirty Thousand and No/100 ($30,000.00) Dollars, cash, this day paid, the receipt whereof is hereby acknowledged, and the balance of Two Hundred and Seventy Thousand & No/100 ($270,000.00) Dollars in installments as follows; Seventy-five Hundred & No/100 ($7,500) Dollars on the first day of March, 1925, and a like sum of $7,500.00 on the first day of each and every third month thereafter until the full balance of $270,000.00 is fully paid; said installments shall bear no interest before maturity, but after maturity said installments shall bear interest at the rate of 8% per annum until paid.

2. As a part of the consideration of the payment of said sums of money, as aforesaid, the party of the second part does hereby agree to sell and transfer to the party of the first part his heirs, or assigns, the five hundred (500) shares of the capital stock of the Industrial Life & Health Insurance Company now owned by the party of the second part.

3. The agreement of the party of the second part to sell and transfer said stock is to be construed as a conditional agreement of sale, to become absolute upon the full payment of the said sum of $300,000.00, according to the tenor and effect of this instrument. As a part of the consideration of the payment of said sum of money by the party of the first part, the party of the second part agrees to resign as Vice-President and as a Director of the Industrial Life & Health Insurance Company, and that his salary as such Vice-President and Director shall cease from the date hereof. The party of the second part has endorsed the certificates of his said shares of stock in blank, and has deposited the same with the party of the first part, and the party of the first part acknowledges the receipt of said certificates of stock, and agrees to hold the same in trust until the several [fol. 18] sums of money herein agreed to be paid by the party of the first part shall have been fully made. Said stock shall not be transferred on the books of the company until the payments herein agreed to be made by the party of the first part have been fully and completely made, but the party of the first part shall have the right to receive all dividends which may be declared and paid on said shares of stock as long as the party of the first part is not in default in the making of the payments herein agreed to be made.

4. Should the party of the first part, or his heirs or assigns make default in any of the above payments, and should said default continue for a period of ninety days, then said shares of stock shall be on demand returned to the party of the second part, and this agreement cancelled, and the party of the second part shall be restored to all of his rights as owner of said shares of stock and any payments which the party of the first part, or his heirs or assigns, may have theretofore paid, shall be forfeited to the party of the second part in consideration of his loss of salary as an officer and director of the company and of the dividends which he would or might have drawn as a stockholder prior to such forfeiture.

In Witness Whereof, the parties hereto have hereunto set their hands and affixed their seals, in duplicate, the day and year first above written.

Signed, sealed and delivered in the presence of: Mrs. J. M. Byrd, H. T. Dobbs, Notary Public. (Seal embossed.) J. N. McEachern, Party of the First Part. (Seal.) S. C. McEachern, Party of the Second Part.

NOTE.—Summons omitted.

[File endorsement omitted.]

[fol. 19] IN UNITED STATES DISTRICT COURT

ANSWER—Filed March 9, 1935

To the District Court of the United States for the Northern District of Georgia, Atlanta Division:

Now comes the defendant and answers the petition on file as follows:

For a First Defense to the First Count

1. Admits the allegations of paragraphs 1, 2, 3, 5, 6, 8, 9, 10, 11, 15, 16 and 18.

2. Denies the allegations of paragraphs 7, 12, 14 and 17.

3. Denies that the defendant is indebted to the plaintiff in the principal sum of $230.07, together with interest at

6% per annum from December 11, 1930, as alleged in paragraph 4, or in any other sum.

4. Denies the allegations of paragraph 13 and further answering says that any action which may have been taken by the Commissioner of Internal Revenue in respect to the Federal estate tax liability of the estate of S. C. McEachern, deceased, neither operates to preclude correct action as to the issues herein involved nor as an admission against this defendant or upon his behalf.

For a Second Defense to the First Count

For a further and second defense to the first count of the petition herein the defendant alleges:

[fol. 20] 1. That S. C. McEachern, the decedent, in his lifetime elected to and did report a gain from the sale, which is described in Exhibit "A" of the petition herein, on the installment basis for the years 1924, 1925, 1926 and 1927 and paid the taxes due thereon.

2. That in the income tax return filed for the decedent, S. C. McEachern, for the year 1928 and in the income tax returns filed for the estate of S. C. McEachern for the years 1929, 1930 and 1931, the plaintiff, with full knowledge of the said decedent's election as set out in paragraph immediately preceding, continued the practice of the decedent by reporting in each of those returns the sale of 50 shares of stock in each year as separate sales thereof.

3. That in the income tax return filed for the decedent for the year 1928 the plaintiff failed to report the fact that an installment obligation existed and to thereby give the Commissioner an opportunity to assess and collect from the estate a tax upon the gain resulting from the transmission thereof by the decedent to the estate under Section 44(d) of the Revenue Act of 1928.

4. That after the assessment of the tax on the gain resulting under Section 44(d) of the Revenue Act of 1928 had become barred by the statute of limitations, the plaintiff filed his claims for refund for the years 1929, 1930 and 1931 therein showing that the stock reported sold in each of said years involved an installment obligation and alleging that the income of the estate and the taxes thereon for the years 1929, 1930 and 1931 were overstated in the returns

as filed for said years, because instead of using the cost to the decedent as the basis for the stock reported sold in said years, the basis should have been the fair market value of the stock at the date of the death of the decedent, the grounds set out in said claims for refund being the grounds which form the basis of this suit.

[fol. 21] 5. That in claiming refunds based on the alleged erroneous returns for 1929, 1930 and 1931 no offer was made to file an amended return for the decedent for 1928 or to pay the tax for that year which should have been paid by the estate on any gain resulting under Section 44(d) of the Revenue Act of 1928.

6. That in view of the conduct of the plaintiff in making the income tax return for the decedent for the year 1928 and in making his tax returns for the years 1929, 1930 and 1931, respectively, in the form and manner as hereinabove alleged and inducing the defendant to accept the same and in accepting the benefits derived therefrom and in view of the acts of the Commissioner in relying in good faith upon and accepting plaintiff's said sworn tax returns as aforesaid for these four years as correct so far as the items of income involved herein are concerned, it would be unconscionable for the plaintiff to be allowed any recovery from the defendant as an overpayment of its 1929 income tax upon the theory that a different basis should be used in determining the gain in connection with the sums collected during the year 1929 under the contract set out as Exhibit "A" of the petition, and thereby leave the defendant without any existing available remedy to enforce collection from the plaintiff of tax that would be due for the year 1928 under the theory which the plaintiff now seeks to advance.

7. That the defendant, the Commissioner of Internal Revenue and the United States relied to their prejudice on plaintiff's position and representation in respect of the manner and method of reporting the income of said estate for the calendar year 1928, and the Commissioner of Internal Revenue and the United States are now precluded from assessing and collecting any tax from plaintiff for said year computed upon the basis which plaintiff now contends is the correct basis for computing said tax liability, and plaintiff is estopped to assert and claim that any [fol. 22] portion of the taxes in controversy in this action

were not taxable to said estate while receiving the benefit resulting from the inability of the United States to collect a tax computed upon what plaintiff now contends is the correct basis.

8. That, by reason of the foregoing, defendant avers that plaintiff is now estopped from changing (for the purpose of recovering from defendant in this action) the position taken in his own sworn tax return for the year 1929 as aforesaid, and said matter of estoppel in pais is expressly relied upon by the defendant and is here placed in bar of plaintiff's recovery in this action of any amount as an overpayment of plaintiff's 1929 tax.

For a First Defense to the Second Count

1. Admits the allegations of paragraphs 1, 2, 3, 5, 6, 8, 9, 10, 11, 15, 16, 17 and 19.

2. Denies the allegations of paragraphs 7, 12 and 14.

3. Denies that the defendant is indebted to the plaintiff in the principal sum of $1,951.61, with interest at six per cent per annum on $434.62 from March 16, 1931, on $434.62 from June 11, 1931, on $434.62 from September 11, 1931, on $647.75 from December 15, 1931, as alleged in paragraph 4, or in any other sum.

4. Denies the allegation of paragraph 18 that $38.59 is the correct amount which the gross income received by the estate of S. C. McEachern for the year 1930 exceeded the deductions properly allowable to said estate in the year 1930, and further denies that the net income for the year 1930 was offset by the allowable exception as alleged in said paragraph.

[fol. 23] 5. Denies the allegations of paragraph 13 and further answering says that any action which may have been taken by the Commissioner of Internal Revenue in respect to the Federal estate tax liability of the estate of S. C. McEachern, deceased, neither operates to preclude correct action as to the issues herein involved nor as an admission against this defendant or upon his behalf.

For a Second Defense to the Second Count

For a further and second defense to the second count of the petition herein the defendant alleges:

1. That S. C. McEachern, the decedent, in his lifetime elected to and did report a gain from the sale, which is described in Exhibit "A" of the petition herein, on the installment basis for the years 1924, 1925, 1926 and 1927 and paid the taxes due thereon.

2. That in the income tax return filed for the decedent, S. C. McEachern, for the year 1928 and in the income tax returns filed for the estate of said S. C. McEachern for the years 1929, 1930 and 1931, the plaintiff, with full knowledge of the said decedent's election as set out in the paragraph immediately preceding, continued the practice of the decedent by reporting in each of those returns the sale of 50 shares of stock in each year as separate sales thereof.

3. That in the income tax return filed for the decedent for the year 1928 the plaintiff failed to report the fact that an installment obligation existed and to thereby give the Commissioner an opportunity to assess and collect from the estate a tax upon the gain resulting from the transmission thereof by the decedent to the estate under Section 44(d) of the Revenue Act of 1928.

[fol. 24] 4. That after the assessment of the tax on the gain resulting under Section 44(d) of the Revenue Act of 1928 had become barred by the statute of limitations, the plaintiff filed his claims for refund for the years 1929, 1930 and 1931 therein showing that the stock reported sold in each of said years involved an installment obligation and alleging that the income of the estate and the taxes thereon for the years 1929, 1930 and 1931 were overstated in the returns as filed for said years, because instead of using the cost to the decedent as the basis for the stock reported sold in said years, the basis should have been the fair market value of the stock at the date of the death of the decedent, the grounds set out in said claims for refund being the grounds which form the basis of this suit.

5. That in claiming refunds based on the alleged erroneous returns for 1929, 1930 and 1931 no offer was made to file an amended return for the decedent for 1928 or to pay the tax for that year which should have been paid by the estate on any gain resulting under Section 44(d) of the Revenue Act of 1928.

6. That in view of the conduct of the plaintiff in making the income tax return for the decedent for the year 1928

and in making his tax returns for the years 1929, 1930 and 1931, respectively, in the form and manner as hereinabove alleged and inducing the defendant to accept the same and in accepting the benefits derived therefrom and in view of the acts of the Commissioner in relying in good faith upon and accepting plaintiff's said sworn tax returns as aforesaid for these four years as correct so far as the items of income involved herein are concerned, it would be unconscionable for the plaintiff to be allowed any recovery from the defendant as an overpayment of its 1930 income tax upon the theory that a different basis should be used in determining the gain in connection with the sums collected during the year 1930 under the contract set out as Exhibit [fol. 25] "A" of the petition, and thereby leave the defendant without any existing available remedy to enforce collection from the plaintiff of tax that would be due for the year 1928 under the theory which the plaintiff now seeks to advance.

7. That the defendant, the Commissioner of Internal Revenue and the United States relied to their prejudice on plaintiff's position and representation in respect of the manner and method of reporting the income of said estate for the calendar year, and the Commissioner of Internal Revenue and the United States are now precluded from assessing and collecting any tax from plaintiff for said year computed upon the basis which plaintiff now contends is the correct basis for computing said tax liability, and plaintiff is estopped to assert and claim that any portion of the taxes in controversy in this action were not taxable to said estate while receiving the benefit resulting from the inability of the United States to collect a tax computed upon what plaintiff now contends is the correct basis.

8. That, by reason of the foregoing, defendant avers that plaintiff is now estopped from changing (for the purpose of recovering from defendant in this action) the position taken in his own sworn tax return for the year 1930 as aforesaid, and said matter of estoppel in pais is expressly relied upon by the defendant and is here pleaded in bar of plaintiff's recovery in this action of any amount as an overpayment of plaintiff's 1930 income tax.

For a First Defense to the Third Count

1. Admits the allegations of paragraphs 1, 2, 3, 5, 10, 11, 12, 13, 17, 18, 19 and 21.

[fol. 26] 2. Denies the allegations of paragraphs 9, 14 and 16.

3. Denies that the defendant is indebted to the plaintiff in the principal sum of $1,676.66, with interest at six per cent per annum on $401.20 from March 15, 1932, on $416.65 from June 17, 1932, on $416.65 from September 15, 1932, on $441.18 from May 31, 1933, and on $1.00 from June 8, 1933, as alleged in paragraph 4, or in any other sum.

4. Denies that the last installment referred to in paragraph 6 was paid on May 31, 1933, and alleges that said installment was paid on June 7, 1933. Admits the remainder of paragraph 6.

5. Denies the allegations of paragraph 7 that May 31, 1933, was the date on which the defendant collected from the plaintiff interest in the sum of $24.54 on the last installment of principal referred to in paragraph 6 of the petition and alleges that said collection was made on June 7, 1933. Denies the further allegation of paragraph 7 that the installment of $416.62 therein referred to was collected on May 31, 1933, and alleges that said collection was made on June 7, 1933.

6. Denies the allegation of paragraph 8 that June 8, 1933, was the date of the interest collection referred to in said paragraph and further denies that May 31, 1933, was the date of the installment collection therein referred to and alleges that June 12, 1933, was the date of said interest collection and that June 7, 1933, was the date of said installment collection.

7. Denies the allegations of paragraph 15 and further answering says that any action which may have been taken by the Commissioner of Internal Revenue in respect to the Federal estate tax liability of the estate of S. C. McEachern, deceased, neither operates to preclude correct [fol. 27] action as the issues herein involved nor as an admission against this defendant or upon his behalf.

8. Denies the allegation of paragraph 20 that $2,529.79 is the correct amount which the gross income received by

the estate of S. C. McEachern in the year 1931 exceeded the deductions properly allowable to said estate in the year 1931, and denies that after the deduction of the permitted exemption from the net income of said year that the sum of $1,029.79 was the correct amount subject to normal tax at the rate of 1½% and further denies that the total normal tax for said year was $15.45.

For a Second Defense to the Third Count

For a further and second defense to the third count of the petition herein the defendant alleges:

1. That S. C. McEachern, the decedent, in his lifetime elected to and did report a gain from the sale, which is described in Exhibit "A" of the petition herein, on the installment basis for the years 1924, 1925, 1926 and 1927 and paid the taxes due thereon.

2. That in the income tax return filed for the decedent, S. C. McEachern, for the year 1928 and in the income tax returns filed for the estate of said S. C. McEachern for the years 1929, 1930 and 1931, the plaintiff with full knowledge of the said decedent's election as set out in the paragraph immediately preceding, continued the practice of the decedent by reporting in each of those returns the sale of 50 shares of stock in each year as separate sales thereof.

3. That in the income tax return filed for the decedent for the year 1928 the plaintiff failed to report the fact that [fol. 28] an installment obligation existed and to thereby give the Commissioner an opportunity to assess and collect from the estate a tax upon the gain resulting from the transmission thereof by the decedent to the estate under Section 44(d) of the Revenue Act of 1928.

4. That after the assessment of the tax on the gain resulting under Section 44(d) of the Revenue Act of 1928 had become barred by the statute of limitations, the plaintiff filed his claims for refund for the years 1929, 1930 and 1931 therein showing that the stock reported sold in each of said years involved an installment obligation and alleging that the income of the estate and the taxes thereon for the years 1929, 1930 and 1931 were overstated in the returns as filed for said years, because instead of using the

cost to the decedent as the basis for the stock reported sold in said years, the basis should have been the fair market value of the stock at the date of the death of the decedent, the grounds set out in said claims for refund being the grounds which form the basis of this suit.

5. That in claiming refunds based on the alleged erroneous returns for 1929, 1930 and 1931 no offer was made to file an amended return for the decedent for 1928 or to pay the tax for that year which should have been paid by the estate on any gain resulting under Section 44(d) of the Revenue Act of 1928.

6. That in view of the conduct of the plaintiff in making the income tax return for the decedent for the year 1928 and in making his tax returns for the years 1929, 1930 and 1931, respectively, in the form and manner as hereinabove alleged and inducing the defendant to accept the same and in accepting the benefits derived therefrom and in view of the acts of the Commissioner in relying in good faith upon and accepting plaintiff's said sworn tax returns as aforesaid for these four years as correct so far [fol. 29] as the items of income herein are concerned, it would be unconscionable for the plaintiff to be allowed any recovery from the defendant as an overpayment of its 1931 income tax upon the theory that a different basis should be used in determining the gain in connection with the sums collected during the year 1931 under the contract set out as Exhibit "A" of the petition, and thereby leave the defendant without any existing available remedy to enforce collection from the plaintiff of tax that would be due for the year 1928 under the theory which the plaintiff now seeks to advance.

7. That the defendant, the Commissioner of Internal Revenue and the United States relied to their prejudice on plaintiff's position and representation in respect of the manner and method of reporting the income of said estate for the calendar year 1928, and the Commissioner of Internal Revenue and the United States are now precluded from assessing and collecting any tax from plaintiff for said year computed upon the basis which plaintiff now contends is the correct basis for computing said tax liability, and plaintiff is estopped to assert and claim that any portion of the taxes in controversy in this action

were not taxable to said estate while receiving the benefit resulting from the inability of the United States to collect a tax computed upon what plaintiff now contends is the correct basis.

8. That, by reason of the foregoing, defendant avers that plaintiff is now estopped from changing (for the purpose of recovering from defendant in this action) the position taken in his own sworn tax return for the year 1931 as aforesaid, and said matter of estoppel in pais is expressly relied upon by the defendant and is here pleaded in bar of plaintiff's recovery in this action of any amount as an overpayment of plaintiff's income tax.

[fol. 30] Wherefore, defendant prays that the petition be dismissed with costs.

Lawrence S. Camp, United States Attorney; M. Neil Andrews, Asst. U. S. Attorney, Attorneys for the Defendant.

Duly sworn to by J. T. Rose. Jurat omitted in printing.

IN UNITED STATES DISTRICT COURT

MOTION FOR DIRECTED VERDICT—Filed April 10, 1935

Now comes the defendant by its Counsel in open Court immediately after the close of all the evidence in the case and moves the Court for a directed verdict in his favor for the following reasons:

[fol. 31] 1. That the pleadings and the evidence are legally insufficient to support any judgment in favor of the plaintiff in the cause.

2. That under the pleadings and the evidence, the plaintiff is estopped to asserting a claim that any portion of the taxes in controversy in this action were not taxable to the estate of S. C. McEachern.

M. Neil Andrews, Assistant United States Attorney; Edward P. Hodges, Special Assistant to the Attorney General, and —— ——, Attorneys for Defendant.

IN UNITED STATES DISTRICT COURT

VERDICT

We, the jury, find for the Plaintiff in the principal sum of $3858.34, with interest at six per cent per annum as provided by law on $230.07 from December 11, 1930, on $434.62 from March 16, 1931, $434.62 from June 11, 1931, on $434.62 from September 11, 1931, on $647.75 from December 15, 1931, on $401.20 from March 15, 1932, on $416.65 from June 17, 1932, on $416.65 from September 15, 1932, on $442.16 from June 12, 1933.

April 11, 1935.

A. E. Wheeler, Foreman.

[fol. 32] IN UNITED STATES DISTRICT COURT

JUDGMENT—Filed April 11, 1935

This case having come on for trial before the Honorable William H. Barrett, United States Judge, and a jury, on April 10, 1935, and the jury having rendered a verdict for Plaintiff on the direction of the Court, it is hereby ordered, adjudged and decreed that the Plaintiff do have and recover from the Defendant the principal sum of $3,858.34, together with interest, as provided by Section 615 of the Revenue Act of 1928, at 6% per annum, from the date of overpayment, to-wit: On $230.07 from December 11, 1930, on $434.62 from March 16, 1931, on $434.62 from June 11, 1931, on $434.62 from September 11, 1931, on $647.75 from December 15, 1931, on $401.20 from March 15, 1932, on $416.65 from June 17, 1932, on $416.65 from September 15, 1932, and on $442.16 from June 12, 1933, together with costs of this proceeding, to-wit, $—.

This 11th day of April, 1935.

Wm. H. Barrett, United States Judge, Designated.

Joseph B. Brennan, Attorney for Plaintiff.

IN UNITED STATES DISTRICT COURT

Bill of Exceptions—Filed August 28, 1935

Be it remembered that on the 10th day of April, 1935, at a regular term of the United States District Court for the

Northern District of Georgia, Atlanta Division, begun and held in the City of Atlanta, the above-entitled cause came on to be tried before the Honorable William H. Barrett, United [fol. 33] States Judge Designate presiding, and a jury. The following appearances were noted: Messrs. Sutherland, Tuttle and Brennan, for the plaintiff; Lawrence S. Camp, United States Attorney, Edward P. Hodges, Special Assistant to the Attorney General, and William B. Waldo, Special Assistant to the Attorney General, for the defendant, when the following proceedings were had, to-wit:

The court being duly organized, the above-entitled case was called for trial and a jury was duly impaneled and sworn.

OFFERS IN EVIDENCE

Plaintiff introduced the following documentary evidence: Income tax returns for 1929, 1930 and 1931, as follows:

Individual Income Tax Return

For Net Incomes from Salaries or Wages of More Than $5,000 and Incomes from Business, Profession, Rents, or Sale of Property

For Calendar Year 1929

File This Return With the Collector of Internal Revenue for Your District on or Before March 15, 1930.

Estate of S. C. McEachern, 507 Kennesaw Avenue, Marietta, Georgia

Occupation—Died Dec. 12, 1928

Income

Item and Instruction No.		
7.	Rents and Royalties. (From Schedule B)	$77.05
8.	Profit from Sale of Real Estate, Stock, Bonds, etc. (From Schedule C)	25,950.00
[fol. 34] 12.	Total Income in Items 1 to 11	$25,672.95

Deductions

Item and Instruction No.		
13.	Interest Paid	$2,050.00
14.	Taxes Paid. (Explain in *in* Schedule F)	1,529.62
19.	Total Deductions in Items 13 to 18	$3,579.62
20.	Net Income (Item 12 minus Item 19)	$22,093.33

Earned Income Credit

21.	Earned Income (not over $30,000)	$5,000.00
22.	Less Personal Exemption and Credit for Dependents	1,500.00
23.	Balance (Item 21 minus 22)	$3,500.00
24.	Amount taxable at 1½% (not over $4,000)	$3,500.00
27.	Normal Tax (1½% of Item 24)	$17.50
31.	Tax on Earned Net Income (total of Items 27 to 30)	$17.50
32.	Credit of 25% of Tax (not over 25% of Items 30, 44, 45 and 46)	$4.37

Computation of Tax

33.	Net Income (Item 20 above)	$22,093.33
37.	Less Personal Exemption	1,500.00
38.	Total of Items 34 to 37	$1,500.00
39.	Balance (Item 33 minus 38)	$20,593.33

[fol. 35]

40.	Amount taxable at 1½% (not over $4,000)	4,000.00
41.	Balance (Item 39 minus 40)	$16,593.33
42.	Amount taxable at 3% (not over $4,000)	4,000.00

Item and Instruction No.		
43.	Amount taxable at 5% (Item 41 minus Item 42)	$12,593.33
44.	Normal Tax (1½% of Item 40)	$20.00
45.	Normal Tax (3% of Item 42)	80.00
46.	Normal Tax (5% of Item 43)	503.73
47.	Surtax on Item 20 (see Instruction 23)	324.67
48.	Tax on Net Income (Total of Items 44 to 47)	$928.40
50.	Total of or difference between Items 48 and 49	$928.40
51.	Less Credit of 25% of Tax on Earned Income (Item 32)	4.37
52.	Total Tax (Item 50 minus 51)	$924.03
55.	Balance of Tax (Item 52 minus Items 53 and 54)	$924.03

Affidavit

I swear (or affirm) that this return, including the accompanying schedules and statements, has been examined by me, and to the best of my knowledge and belief, is a true and complete return made in good faith for the taxable year stated, pursuant to the Revenue Act of 1928 and the Regulations issued thereunder.

D. W. McEachern, Adm.

Sworn to and subscribed to before me this 14th day of March, 1930. (Signature illegible.) Notarial Seal.)

[fol. 36]

Schedule B—Income from Rents and Royalties

1. Kind of Property	2. Amount Received	3. Cost or Value as of March 1, 1913, Whichever Greater	4. Depreciation (Explain in table at foot of page)	5. Repairs	6. Other Expenses (Itemize below)	7. Net Profit (Enter as Item 7)
Brick Store—Marietta, Ga.....	$1,450.00	$15,000.00	$400.00	$350.00	$777.05	$77.05

Explanation of deductions claimed in Column 6.—Insurance, $452.30; Taxes, $324.75.

Schedule C—Profit from Sale of Real Estate, Stocks, Bonds, Etc.

1. Kind of Property	2. Date Acquired	3. Amount Received	5. Cost or Value as of March 1, 1913, Whichever Greater	7. Net Profit (Enter as Item 8)
50 Sh. Ind. Life & H. Ins. Co.....	1918	$26,250.00	$500.00	$25,750.00

[fol. 37]

State how property was acquired.—Cash.

Schedule F—Explanation of Deductions Claimed in Items 1, 14, 16, 17 and 18

Taxes—Inheritance, Ga., $499.37; U. S., $124.85.
Taxes—State & Co., $623.45; Marietta, $217.20; Auto Tags, $64.75.
Total, $1,529.63

Explanation of Deduction for Depreciation Claimed in Schedules A and B

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquirement	5. Cost or Value as of March 1, 1913, Whichever Greater (Exclusive of Land)	Amount of Depreciation Charged off	
					6. Previous years	7. This year
Brick Store.....	1919	8 yrs.	30 yrs.	$12,000.00	$2,000.00	$400.00

[fol. 38] Individual Income Tax Return

For Net Incomes from Salaries or Wages of More Than $5,000 and Incomes from Business, Profession, Rents, or Sale of Property

For Calendar Year 1930

File This Return With the Collector of Internal Revenue for Your District on or Before March 15, 1931.

Estate of S. C. McEachern, 507 Kennesaw Avenue, Marietta, Georgia

Occupation—Died Dec. 12, 1928

2. If you filed a return for 1929, to what Collector's office was it sent? Atlanta, Ga.

Income

Item and Instruction No.			
7.	Rents and Royalties. (From Schedule B)	$665.06	
8.	Profit from Sale of Real Estate, Stocks, Bonds, etc. (From Schedule C)	33,250.00	
12.	Total Income in Items 1 to 11		$33,915.06

Deductions

13.	Interest Paid	$1,920.00	
14.	Taxes Paid. (Explain in Schedule F)	1,631.36	
16.	Bad Debts. (Explain in Schedule F)	1,389.79	

[fol. 39]

19.	Total Deduction in Items 13 to 18	$4,941.15
20.	Net Income (Item 12 minus Item 19)	$28,973.91

Earned Income Credit

Item and Instruction No.	
21. Earned Income (not over $30,000)	$5,000.00
22. Less Personal Exemption and Credit for Dependents	1,500.00
23. Balance (Item 21 minus 22)	$3,500.00
24. Amount taxable at 1½% (not over $4,000)	$3,500.00
27. Normal Tax (1½% of Item 24)	$52.50
31. Tax on Earned Net Income (total of Items 27 to 30)	$52.50
32. Credit of 25% of Tax (not over 25% of Items 30, 44, 45 and 46)	$13.12

Computation of Tax

33. Net Income (Item 20 above)		$28,973.91
37. Less Personal Exemption	$1,500.00	
38. Total of Items 34 to 37		1,500.00
39. Balance (Item 33 minus 38)		$27,473.91
40. Amount taxable at 1½% (not over $4,000)		4,000.00
41. Balance (Item 39 minus 40)		$23,473.91
42. Amount taxable at 3% (not over $4,000)		4,000.00

[fol. 40]

43. Amount taxable at 5% (Item 41 minus 42)	$19,473.91
44. Normal Tax (1½% of Item 40)	$60.00
45. Normal Tax (3% of Item 42)	120.00
46. Normal Tax (5% of Item 43)	973.70
47. Surtax on Item 20 (see Instruction 23)	797.91
48. Tax on Net Income (total of Items 44 to 47)	$1,951.61

Item and Instruction No.		
50.	Total of or difference between Items 48 and 49	$1,951.61
52.	Total Tax (Item 50 minus 51)	$1,936.49
55.	Balance of Tax (Item 52 minus Items 53 and 54)	$1,936.49

Taxpayer's Record of Payments

Payment	Amount	Date	Check or M. O. No.	Bank or Office of Issue
Second	14 Willis Dobbs	March		D. W. McEachern, Admin. Marietta, Ga.

[fol. 41]

Schedule B—Income From Rents and Royalties

1. Kind of Property	2. Amount Received	3. Cost or Value as of March 1, 1913, Whichever Greater	4. Depreciation (Explain in table at foot of page)	5. Repairs	6. Other Expenses (Itemize below)	7. Net Profit (Enter as Item 7)
Brick Store—Marietta, Ga.....	$1,430.00	$15,000.00	$378.00	.....	$386.94	$665.06

Explanation of deductions claimed in Column 6.—Taxes, $330.00; Water, $56.94.

Schedule C—Profit from Sale of Real Estate, Stocks, Bonds, Etc.

1. Kind of Property	2. Date Acquired	3. Amount Realized	5. Cost or Value as of March 1, 1913, Whichever Greater	7. Net Profit (Enter as Item 8)
50 Sh. Ind. L. & H. Ins. Co.....	1918	$33,750.00	$500.00	$33,250.00

[fol. 42]

Schedule F—Explanation of Deductions Claimed in Items 1, 14, 16, 17 and 18

14—Taxes, City, State and County, on real estate and personal, $1,545.62—Ga. Income Tax, $85.74.
16—Notes, W. O. Beatner, endorsed by S. C. McEachern, paid by Estate—Uncollectible.

Explanation of Deduction for Depreciation Claimed in Schedules A and B

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquirement	5. Cost or Value as of March 1, 1913, Whichever Greater (Exclusive of Land)	Amount of Depreciation Charged off	
					6. Previous years	7. This year
Brick Store.....	1919	8 yrs.	30 yrs.	$12,600.00	$2,400.00	$378.00
Additional improvements 1929 of $600.00.						

[fol. 43] Individual Income Tax Return

For Net Incomes from Salaries or Wages of More than $5,000 and Incomes from Business, Profession, Rents, or Sale of Property

For Calendar Year 1931

File This Return With the Collector of Internal Revenue for Your District on or Before March 15, 1932.

Estate of S. C. McEachern, 507 Kennesaw Avenue, Marietta, Georgia

2. If you filed a return for 1930, to what Collector's office was it sent? Atlanta, Ga.

Income

Item and Instruction No.			
7.	Rents and Royalties. (From Schedule B)	$73.95	
8.	Profit from Sale of Real Estate, Stocks, Bonds, etc. (From Schedule C)	29,500.00	
12.	Total Income in Items 1 to 11		$29,426.05

Deductions

13.	Interest Paid	$1,220.00	
14.	Taxes Paid. (Explain in Schedule F)	1,426.31	
[fol. 44] 15.	Losses by Fire, Storm etc. (Explain in Table at foot of page 2)	100.00	
19.	Total Deductions in Items 13 to 18		$2,746.31
20.	Net Income (Item 12 minus Item 19)		$26,679.74

Computation of Tax

Item and Instruction No.		
33. Net Income (Item 20 above)		$26,679.74
37. Less Personal Exemption	$1,500.00	
38. Total of Items 34 to 37		$1,500.00
39. Balance (Item 33 minus 38)		$25,179.74
40. Amount taxable at 1½% (not over $4,000)		4,000.00
41. Balance (Item 39 minus 40)		$21,179.74
42. Amount taxable at 3% (not over $4,000)		4,000.00
43. Amount taxable at 5% (Item 41 minus 42)		$17,179.74
44. Normal Tax (1½% of Item 40)		$60.00
45. Normal Tax (3% of Item 42)		120.00
46. Normal Tax (5% of Item 43)		858.99
47. Surtax on Item 20 (see Instruction 23)		627.56
48. Tax on Net Income (total of Items 44 to 47)		$1,666.57
50. Total of or difference between Items 48 and 49		$1,666.57
52. Total Tax (Item 50 minus 51)		$1,666.57
[fol. 45] 55. Balance of Tax (Item 52 minus Items 53 and 54)		$1,666.57

Taxpayer's Record of Payments

Payment	Amount	Date	Check or M. O. No.	Bank or Office of Issue
Second.....	15 (Signature illegible)	March		Estate of S. C. McEachern By D. W. McEachern, Administrator, Marietta, Ga.

[fol. 46] Schedule B—Income from Rents and Royalties

1. Kind of Property	2. Amount Received	3. Cost or Value as of March 1, 1913, Whichever Greater	4. Depreciation (Explain in table at foot of page)	5. Repairs	6. Other Expenses (Itemize below)	7. Net Profit (Enter as Item 7)
Brick Store—Marietta, Ga.....	$1,560.00.	$15,000.00	$420.00	$98.75	$1,115.20	$73.95

Explanation of deductions claimed in Column 6.—City & S. & Co. taxes, $322.50—Water, $56.70 Int., $336.00—Fire Ins., $400.90.

Schedule C—Profit from Sale of Real Estate, Stocks, Bonds, Etc.

1. Kind of Property	2. Date Acquired	3. Amount Realized	5. Cost or Value as of March 1, 1913, Whichever Greater	7. Net Profit (Enter as Item 8)
50 Shs. Ind. L. & H. Ins. Co.....	1918	$30,000.00	$500.00	$29,500.00

[fol. 47] Schedule F—Explanation of Deductions Claimed in Items 1, 14, 16, 17 and 18

14—State & Co. $516.63—City $263.50 on real. & Per.—Ga. State Tax $646.16 on Inc. Total, $1,426.31.

Explanation of Deduction for Depreciation Claimed in Schedules A and B

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquirement	5. Cost or Value as of March 1, 1913, Whichever Greater (Exclusive of Land)	Amount of Depreciation Charged off	
					6. Previous years	7. This year
Brick Store.....	1919	8 yrs.	30 yrs.	$12,600.00	$2,778.00	$420.00

Explanation of Deduction for Losses by Fire, Storm, Etc., Claimed in Schedule A, and in Item 15

1. Kind of Property	7. Deductible Loss
Burglar broke down doors and damaged store. Cost of repairs.....	$100.00

[fol. 48] Amended Individual Income Tax Return

For Net Incomes from Salaries or Wages of More Than $5,000 and Incomes from Business, Profession, Rents, or Sale of Property

For Calendar Year 1931

File This Return With the Collector of Internal Revenue for Your District on or Before March 15, 1932.

Estate of S. C. McEachern, 507 Kennesaw Avenue, Marietta, Georgia

2. If you filed a return for 1930, to what Collector's office was it sent? Alanta, Ga.

Income

Item and Instruction No.			
4.	Interest on Tax-free Covenant Bonds Upon Which a Tax was Paid at Source	$4,999.95	
7.	Rents and Royalties. (From Schedule B)	73.95	
12.	Total Income in Items 1 to 11		$4,926.00

Deductions

13.	Interest Paid	$1,220.00	
14.	Taxes Paid. (Explain in Schedule F)	1,426.31	
[fol. 49] 15.	Losses by Fire, Storm, etc. (Explain in Table at foot of page 2)	100.00	
19.	Total Deductions in Items 13 to 18		$2,746.31
20.	Net Income (Item 12 minus Item 19)		$2,179.69

Earned Income Credit

Item and Instruction No.		
21. Earned Income (not over $30,000)		$2,179.69
22. Less Personal Exemption and Credit for Dependents		1,500.00
23. Balance (Item 21 minus 22)		$679.69
24. Amount taxable at 1½% (not over $4,000)		$679.69
27. Normal Tax (1½% of Item 24)		$10.19
31. Tax on Earned Net Income (total of Items 27 to 30)		$10.19
32. Credit of 25% of Tax (not over 25% of Items 30, 44, 45 and 46)		$2.54

Computation of Tax

33. Net Income (Item 20 above)		$2,179.69
37. Less Personal Exemption	$1,500.00	
38. Total of Items 34 to 37		$1,500.00
39. Balance (Item 33 minus 38)		$679.69
40. Amount taxable at 1½% (not over $4,000)		679.69
[fol. 50] 44. Normal Tax (1½% of Item 40)		$10.19
48. Tax on Net Income (total of Items 44 to 47)		$10.19
51. Less Credit of 25% of Tax on Earned Income (Item 32)		2.54
52. Total Tax (Item 50 minus 51)		$7.65
53. Less Income Tax Paid at Source		1,249.95
Overpaid		$1,242.30

Affidavit

I swear (or affirm) that this return, including the accompanying schedules and statements, has been examined by

me, and to the best of my knowledge and belief, is a true and complete return made in good faith for the taxable year stated, pursuant to the Revenue Act of 1928 and the Regulations issued thereunder.

D. W. McEachern, Administrator of the Estate of S. C. McEachern, 704 Kennesaw Ave., Marietta, Ga.

Sworn to and subscribed before me this 8th day of December, 1932. Audrey Taylor, Notary Public. (Notarial Seal.)

[fol. 51] PLAINTIFF'S EXHIBIT No. 4

Stipulation

It is hereby stipulated by and between the parties to the above entitled cause, by their respective attorneys, that the following facts may be taken as true on the trial of said case, subject to the right of either party to object to any of the stipulated facts on grounds of irrelevancy or immateriality, and subject further to the right of either of the parties to introduce other and further evidence not inconsistent with any of the facts herein stipulated to be true.

1

On December 12, 1929, Plaintiff, as Administrator of the Estate of S. C. McEachern, Deceased, filed with the defendant, Collector of Internal Revenue at Atlanta, Georgia, the Federal Estate Tax Return required for said Estate. Said return was filed on the prescribed form furnished by the Treasury Department, namely, Form 706, revised January, 1929. The Federal Estate Tax shown to be due on said return was paid to said Collector on December 12, 1929.

2

Schedule C of said return as filed contained the following entry:

"Unpaid balance of deferred payments on 250 shares of stock of Industrial Life & Health Insurance Company under contract between S. C. McEachern and J. N. McEachern, as Trustee, dated September 3, 1924, $125,000.00."

[fol. 52] This amount of $125,000.00 was included in the gross estate on which estate tax was paid.

3

On the date of the death of S. C. McEachern, the unpaid installment obligations under the contract of September 3, 1924, a true copy of which is attached to the petition marked Exhibit A, were of a face value of $150,000.00, and had a fair market value of $125,000.00, and one-half of the 500 shares of stock in Industrial Life & Health Insurance Company covered by said contract, namely, 250 shares of said stock also had a fair market value of $125,000.00 on said date of the death of the said S. C. McEachern.

4

The fair market value on December 12, 1928 of the unpaid installment obligations described in paragraph 3 was the face amount of said obligations less a discount figured at 6.348% per annum from said date of death to the due date of each of said installments, and the valuation of $125,000.00 for the total of the obligations then outstanding was arrived at by deducting from the face amount of the entire unpaid obligations at said date of death the discount of 6.348% per annum from said date of death to the due date of each of the installments.

5

The total amount collected by Plaintiff in 1929 under the contract of September 3, 1924, copy of which is attached to the petition marked Exhibit A, was $26,250.00 the average collection date of which was seven and one-half months after the date of the death of said S. C. McEachern on December 12, 1928.

6

If the gain derived by said Estate of S. C. McEachern [fol. 53] from the collection in 1929 of said installment obligations in the face amount of $26,250.00, as described in paragraph 5, should be determined by deducting from the total amount of said collections in the sum of $26,250.00 the fair market value at the date of death of said S. C. McEachern of said obligations collected in 1929, the gain would be $952.49, and accordingly the tax would have been overpaid by the Plaintiff in the sum of $924.03, against which the statute of limitations had run at the time of the filing of the claim for refund on all except $230.07, which

said amount of $230.07 with interest from December 11, 1930 is the amount for which judgment should be given for the Plaintiff on the First Count, if Plaintiff is entitled to judgment. Nothing contained in this paragraph shall be taken as an admission by Defendant that Plaintiff is entitled to any judgment whatsoever. The above simply represents the correct figures upon which judgment may be based in the event Plaintiff is entitled to judgment.

7

In the income tax return for the Estate of S. C. McEachern for the year 1929 under the heading "Income," the following entry is found on line 8: "Profit from sale of real estate, stocks, and bonds, $25,750.00," and Schedule C of said return is as follows:

Schedule C—Profit from Sale of Real Estate, Stocks, Bonds, Etc.
(See Instruction 8)

1. Kind of Property	2. Date Acquired	3. Amount Received	4. Depreciation Allowable since Acquisition
50 Sh. Ind. Life & H. Ins. Co.	1918	$26,250.00	.....

[fol. 54]

5. Cost or Value as of Mar. 1, 1913 Whichever Greater	6. Subsequent Improvements	7. Net Profit (Enter as Item 8)	State how Property Was Acquired
$500.00	.....	$25,750.00	Cash

8

The only items of gross income as defined in Section 22 of the Revenue Act of 1928 received by or on behalf of said Estate of S. C. McEachern in the year 1929 were (a) an item of rents received amounting to $247.70 and (b) an item of gain derived from the collection in 1929 of installments in the sum of $26,250.00 under the contract of September 3, 1924, a copy of which is attached to the petition marked Exhibit A. No admission is made in this paragraph by either side as to the proper amount of gain or profit resulting from said collection in 1929.

9

The total amount collected by Plaintiff in 1930 under the contract of September 3, 1924, copy of which is attached to the petition marked Exhibit A, was $33,750.00, the average collection date of which was nineteen and one-half months after the date of the death of said S. C. McEachern on December 12, 1928.

10

If the gain derived by said Estate of S. C. McEachern from the collection in 1930 of said installment obligations in the face amount of $33,750.00, as described in paragraph 9, should be determined by deducting from the total amount of said collections in the sum of $33,750.00 the fair market value at the date of death of said S. C. McEachern of said obligations collected in 1930, the gain would be $3,333.32, and accordingly the tax would have been overpaid by the Plaintiff in the sum of $1,951.61, for which last mentioned [fol. 55] amount judgment should be given for the Plaintiff on the Second Count, if Plaintiff is entitled to judgment, together with interest at six per cent per annum on the following amounts from the following dates:

On $434.62 from March 16, 1931
On 434.62 from June 11, 1931
On 434.62 from September 11, 1931
On 647.75 from December 15, 1931

Nothing contained in this paragraph shall be taken as an admission by Defendant that Plaintiff is entitled to any judgment whatsoever. The above simply represents the correct figures upon which judgment may be based in the event Plaintiff is entitled to judgment.

11

In the income tax return for the Estate of S. C. McEachern for the year 1930 under the heading "Income," the following entry is found on Line 8: "Profit from Sale of Real Estate, Stocks, Bonds, etc., $33,250.00," and Schedule C of said return is as follows:

Schedule C—Profit from Sale of Real Estate, Stocks, Bonds, Etc.
(See Instruction 8)

1. Kind of Property	2. Date Acquired	3. Amount Received
50 Sh. Ind. L. & H. Ins. Co.	1918	$33,750.00

4. Depreciation Allowable since Acquisition	5. Cost or Value as of Mar. 1913, Whichever Greater
.....	$500.00

[fol. 56]

6. Subsequent Improvements	7. Net Profit (Enter as Item 8)
.....	$33,250.00

12

The only items of gross income as defined in Section 22 of the Revenue Act of 1928 received by or on behalf of said Estate of S. C. McEachern in the year 1930 were (a) an item of rents received amounting to $995.06 and (b) an item of gain derived from the collection in 1930 of installments in the sum of $33,750.00 under the contract of September 3, 1924, a copy of which is attached to the petition marked Exhibit A. No admission is made in this paragraph by either side as to the proper amount of gain or profit resulting from said collection in 1930.

13

The total amount collected by Plaintiff in 1931 under the contract of September 3, 1924, copy of which is attached to the petition marked Exhibit A, was $30,000.00, the average collection date of which was thirty-one and one-half months after the date of the death of said S. C. McEachern on December 12, 1928.

14

If the gain derived by said estate of S. C. McEachern from the collection in 1931 of said installment obligations in the face amount of $30,000.00, as described in paragraph 13, should be determined by deducting from the total amount

of said collections in the sum of $30,000.00 the fair market value at the date of death of said S. C. McEachern of said obligations collected in 1931, the gain would be $4,999.95, and accordingly the tax would have been overpaid by the Plaintiff in the sum of $1,676.66, for which last mentioned [fol. 57] amount judgment should be given for the Plaintiff on the Third Count, if Plaintiff is entitled to judgment, together with interest at six percent per annum on the following amounts from the following dates:

On $401.20 from March 15, 1932
On 416.65 from June 17, 1932
On 416.65 from September 15, 1932
On 442.16 from June 12, 1933

Nothing contained in this paragraph shal be taken as an admission by Defendant that Plaintiff is entitled to any judgment whatsoever. The above simply represents the correct figures upon which judgment may be based in the event Plaintiff is entitled to judgment.

15

In the income tax return for the Estate of S. C. McEachern for the year 1931 under the heading "Income," the following entry is found on Line 8: "Profit from Sale of Real Estate, Stocks, Bonds, etc., $29,500.00," and Schedule C of said return is as follows:

Schedule C—Profit from Sale of Real Estate, Stocks, Bonds, Etc.

1. Kind of Property	2. Date Acquired	3. Amount Received
50 Shs. Ind. L. & H. Ins. Co.	1918	$30,000.00

4. Depreciation Allowable since Acquisition	5. Cost or Value as of Mar. 1913, Whichever Greater
.....	$500.00

[fol. 58]

6. Subsequent Improvements	7. Net Profit (Enter as Item 8)
.....	$29,500.00

16

The only items of gross income as defined in Section 22 of the Revenue Act of 1928 received by or on behalf of said Estate of S. C. McEachern in the year 1931 were (a) an item of rents received amounting to $248.54 and (b) an item of gain derived from the collection in 1931 of installments in the sum of $30,000.00 under the contract of September 3, 1924, a copy of which is attached to the petition marked Exhibit A. No admission is made in this paragraph by either side as to the proper amount of gain or profit resulting from said collection in 1931.

17

Nothing herein contained shall be taken as a waiver by either party as to the right to costs.

In Witness Whereof the Attorneys of record of the parties hereof have hereunto set their hands this 10th day of April, 1935.

(Signed) W. A. Sutherland, Joseph B. Brennan, Attorneys for Plaintiff. Neil Andrews, Assistant United States Attorney; Edward P. Hodges, Special Assistant Attorney General, Attorneys for Defendant.

The following occurred after the stipulation was read by Mr. Sutherland:

[fol. 59] Mr. Hodges: I object to paragraphs Nos. 1 and 2 of the stipulation read by attorney for the Plaintiff on the ground that they are immaterial and irrelevant for the following reasons:

1. That which happened in regard to the estate tax return has no bearing on the case involved here, for the reason that estate tax returns and income tax returns are handled by separate and distinct units in the Bureau of Internal Revenue.

2. It was taxpayer's duty to make full and complete showing in his income tax return for 1928 of all income upon which tax was payable in that year.

3. The estate tax return cannot be considered as supplemental to the income tax return for the year of taxpayer's death or for any other year.

In regard to paragraph 8, which has just been read, and also paragraphs 12 and 16, the parties have agreed that, in so far as those paragraphs are in conflict with the returns that have just been introduced in evidence, that they shall be disregarded.

Mr. Sutherland: We agree to that, Your Honor.

The Court overruled the objections of the defendant to the admissibility of paragraphs 1 and 2 of the stipulation offered by the plaintiff and designated "Plaintiff's Exhibit 4." Said exhibit was received in evidence, whereupon the Defendant excepted to the ruling of the Court, and his exception was allowed.

The Plaintiff's evidence closed.

[fol. 60] Mr. Hodges: We offer in evidence the Defendant's stipulation designated as "Defendant's Exhibit A," which reads as follows:

DEFENDANT'S EXHIBIT A

Stipulation

It is hereby stipulated by and between the parties to the above entitled cause, by their respective attorneys, that the following facts may be taken as true on the trial of said case, subject to the right of either party to object to any of the stipulated facts on grounds of irrelevancy or immateriality, and subject further to the right of either of the parties to introduce other and further evidence not inconsistent with any of the facts herein stipulated to be true.

1

On March 12, 1929, Plaintiff as Administrator of the Estate of S. C. McEachern, Deceased, filed with the Collector of Internal Revenue at Atlanta, Georgia, an income tax return on behalf of said S. C. McEachern for the period January 1, 1928, to December 12, 1928. The income tax due according to said return was $1,441.70 which was paid to the Collector in the following amounts on the following dates:

March 12, 1929	$360.43
June 7, 1929	360.43
September 2, 1929	360.43
December 16, 1929	360.41

2

In the return described in paragraph 1 under the heading "Income," Line 6 is as follows: "Profit from sale of [fol. 61] Real Estate, Stocks, Bonds, Etc., $29,500.00," and Schedule C of said return is as follows:

Schedule C—Profit from Sale of Real Estate, Stocks, Bonds, Etc.

(See Instruction 6)

1. Kind of Property	2. Date Acquired	3. Amount Received
50 Shs. Ind. Life & H. Ins. Co.	1918	$30,000.00

4. Depreciation Allowable Since Acquisition	5. Cost	6. Value as of March 1, 1913
.....	$500.00	.....

7. Subsequent Improvements	8. Net Profit (Enter as Item 6)
.....	$29,500.00

3

In the return described in paragraph 1, Plaintiff did not include any gain or profit resulting from the transmission by death from the said S. C. McEachern, Deceased, to his estate of the installment obligations unpaid under the contract of September 3, 1924, a copy of which is attached to petition marked Exhibit "A." If Section 44 (d) of the Revenue Act of 1928 should be held constitutional and applicable for determining a gain on the transmission of the said unpaid installment obligations on the death of S. C. McEachern, then an additional tax in the sum of $11,625.00 would be due and unpaid by the Administrator of the Estate of S. C. McEachern on account of the income tax liability [fol. 62] of said S. C. McEachern for the period from January 1, 1928, to December 12, 1928; provided that the stock in Industrial Life & Health Insurance Company, covered by the contract above referred to had a basis of $10.00 per share in the hands of said S. C. McEachern. $10.00 per share is the basis used by S. C. McEachern in his returns for the years prior to 1928 and by the Administrator of S. C. McEachern in the return filed by him for said S. C. McEachern for 1928. Nothing in this paragraph shall be

taken as an admission that any gain or profit actually resulted from the transmission of said installment obligations by said S. C. McEachern upon his death.

In Witness Hereof the Attorneys of record of the parties hereof have hereunto set their hands this 10th day of April, 1935.

(Signed) W. A. Sutherland, Joseph B. Brennan, Attorneys for Plaintiff. Neil Andrews, Assistant United States Attorney; Edward P. Hodges, Special Assistant to the Attorney General, Attorneys for Defendant.

Mr. Brennan: If Your Honor please, we object to the introduction in evidence of all the facts set forth in that stipulation. We have admitted that they are true, but we do not think they are relevant and material, and we reserved the right to make that objection in signing the stipulation. The particular grounds as to relevancy and materiality [fol. 63] would be as follows: The income tax return filed for the defendant for the year in which he died, to-wit, 1928, can have nothing to do with Plaintiff's income tax liability for 1929, 1930 and 1931, which are the only years in this suit. * * * We contend, in support of our objections to the relevancy and materiality of the stipulation as offered by the Government, that their return, filed on behalf of the decedent for the period from January 1, 1928, to December 12, 1928, the date of his death, cannot serve as an element of estoppel against his estate, which is considered a different taxable entity. * * * As a further ground, we urge that this section 44d of the Revenue Act of 1928, under which the stipulation sets up an additional tax would be derived from the decedent for 1928 under certain circumstances, is not to be construed as applying retroactively and cover the transmission by death in 1928 of installment obligations under a contract of sale executed in 1924. * * * We further urge that if Section 44d of the 1928 Act should be construed as applying to the transmission of these obligations on the death of S. C. McEachern in 1928, then that section is unconstitutional. * * * Plaintiff objects further to the admission in evidence of each and every fact set forth in the stipulation offered by Defendant on the ground that all of said facts are offered solely in support of a defense of estoppel, a necessary and essential element of which is an alleged tax

liability against Plaintiff's intestate for the year of his death, namely, 1928, based upon Section 44d of the Revenue Act of 1928, which Plaintiff contends is unconstitutional for the following reasons:

1. No income can be said to result within the meaning of the Sixteenth Amendment to the Constitution to S. C. McEachern by reason of the transmission by his death of in-[fol. 64] stallment obligations held by him at the date of his death and Section 44d of the 1928 Act in attempting to impose a tax upon such supposed income is inconstitutional and void.

2. Section 44d of the 1928 Act undertakes to measure a gain to the vendor by the value of the deferred obligations at the time of their disposal or transmission, rather than as of the date of the sale. In many instances the value of installment obligations will have increased between the date of sale and the date of the death of the vendor, and in such cases Section 44d would, by its terms, tax this increase in value as a profit to the vendor for the last year of his life, although he received nothing from the disposition of the property. The Sixteenth Amendment does not authorize such a tax.

3. Section 44d is so arbitrary and unreasonably retroactive as to render it unconstitutional under the Fifth Amendment to the Constitution. In undertaking to apply that section in the present case, the Government seeks to impose a tax for 1928 either on a fictitious profit from the transmission of installment obligations by death, or upon a sale made in 1924, at a time when existing law made no provision for such a tax.

The Court stated that he would not pass upon the constitutionality of Section 44d of the Revenue Act of 1928, but he would sustain Plaintiff's objection to the introduction of Defendant's stipulation designated as "Exhibit A" in evidence, on the ground that the facts covered by the stipulation were irrelevant in that they undertook to support a defense of estoppel, and even though the stipulation were admitted, estoppel would not be established. Whereupon the Defendant excepted, and an exception was allowed.

The evidence for the Defendant closed.

[fol. 65] COLLOQUY

Mr. Sutherland: It is agreed between the parties that the estate tax return referred to in paragraph one of the stipulation offered by Plaintiff, was investigated with the usual care by Agent Pratt, in the office of the Internal Revenue Agent at Atlanta, and report of such investigation was made by said agent under date of May 31st, 1930, and transmitted to the Bureau in Washington on the same date.

Mr. Hodges: The defendant admits the truth of that statement, but objects on the same grounds as to paragraphs one and two of Plaintiff's stipulation designated as "Plaintiff's Exhibit 4," inasmuch as it was the duty of the taxpayer to make a full income tax return and not treat his estate tax return as being supplemental to his income tax return.

Mr. Sutherland: I understand there is no question about the good intention and good faith of everybody connected with these transactions in which these returns were prepared and filed throughout.

Mr. Hodges: Well, the Government will not contend that this was done maliciously.

The Court: What do you mean by "maliciously?" Do you mean to say that you agree that it was not done dishonestly and unfairly and was just merely incorrectly made because of not knowing the law as you know it?

[fol. 66] Mr. Hodges: That is right. In other words, we do not impugn his honesty.

The Court: All right, it was either a mistaken return, I mean from any sense that he intended to make a return that revealed the facts which he understood were proper to be revealed.

Mr. Hodges: Yes, sir.

The Court overruled the Defendant's objections and admitted the said oral stipulation in evidence, to which ruling and judgment of the Court the Defendant then excepted, and his exception was duly allowed.

Both sides closed.

Mr. Sutherland, for the Plaintiff, made a motion to direct a verdict in favor of the plaintiff.

Mr. Hodges, for the Government, made a motion to direct a verdict in favor of the Defendant, as follows:

"DEFENDANT'S MOTION FOR DIRECTED VERDICT

Now comes the defendant by its counsel in open Court immediately after the close of all the evidence in the case and moves the Court for a directed verdict in his favor for the following reasons:

1. That the pleadings and the evidence are legally insufficient to support any judgment in favor of the Plaintiff in the cause.

2. That under the pleadings and the evidence, the Plain-
[fol. 67] tiff is estopped to asserting a claim that any portion of the taxes in controversy in this action were not taxable to the estate of S. C. McEachern."

The Court then announced that he would sustain the Plaintiff's motion for a directed verdict, and would overrule Defendant's motion for a directed verdict, whereupon the Defendant excepted and his exception was allowed.

Thereupon the Court directed a verdict in favor of the Plaintiff, and overruled Defendant's motion for a directed verdict, and the jury returned the verdict in accordance with said direction. Thereupon the Defendant, in the presence of the jury, duly excepted to the verdict of the jury, and the exception was allowed.

Thereafter on to-wit, the 11th day of April, 1935, the Court duly entered a judgment and signed a certificate of probable cause therein, to which action by the Court the defendant excepted and his exceptions were allowed.

Thereafter, on the 6th day of May, 1935, the Defendant filed his motion for new trial, and the same was, after consideration thereof by the Court, overruled by the Court on the 16th day of May, 1935, to which judgment so overruling said motion the Defendant duly excepted, and his exception was allowed.

Thereafter, on the 20th day of June, 1935, upon the application of the Defendant and for good cause shown, the Court granted until the 1st day of September, 1935, within which Defendant should make and file a bill of exceptions in said cause.

The foregoing constitutes all the evidence and recites all the material proceedings upon the trial of said cause.

Now, in furtherance of justice and that right may be [fol. 68] done, the Defendant, J. T. Rose, Former Collector of Internal Revenue for the District of Georgia, presents the foregoing as and for his bill of exceptions in the above-entitled cause, and prays that the same may be settled, allowed, signed, and filed as such.

Lawrence S. Camp, United States Attorney; M. Neil Andrews, Asst. United States Attorney, Attorneys for Defendant.

In United States District Court

Stipulation as to Bill of Exceptions

The undersigned, Sutherland, Tuttle and Brennan, for and on behalf of the Plaintiff in the above-entitled cause, do hereby acknowledge service of the above and foregoing bill of exceptions this 22d day of August, 1935, and, having examined the same, do agree that the same is true and correct and that the same may be allowed, settled, signed and filed, and made a part of the record in said cause, and do hereby waive the right to be present at the settling and allowance of said bill of exceptions.

Sutherland, Tuttle & Brennan, Attorneys for Plaintiff.

In United States District Court

Order Settling Bill of Exceptions

Whereupon on the 26th day of August, 1935, upon due notice to said Plaintiff and within the time limited and granted by the Court therefor, the foregoing bill of exceptions is duly tendered by J. T. Rose, Former Collector of Internal Revenue for the District of Georgia, Defendant, [fol. 69] for signing, settlement and allowance as the bill of exceptions in said cause, and the said Plaintiff and Defendant having agreed that the same is true and correct;

It is Ordered that the above and foregoing be and the same is herewith duly signed, certified and allowed as the bill of exceptions in said cause, and as being true and correct, and the same is hereby made a part of the record in said cause and ordered filed as such.

Done this 26th day of August, 1935.

Wm. H. Barrett, United States District Judge Designate.

IN UNITED STATES DISTRICT COURT

PETITION FOR APPEAL—Filed August 14, 1935

To the Honorable William H. Barrett, United States Judge Designate:

Comes now on this 9th day of August, 1935, appellant J. T. Rose, former Collector of Internal Revenue, by his attorneys, Lawrence S. Camp, United States Attorney, and M. Neil Andrews, Assistant United States Attorney, and feeling aggrieved by the judgment of the Court made and entered in this case on the 11th day of April, 1935, does hereby appeal from said judgment to the Circuit Court of Appeals for the Fifth Circuit, for the reasons specified in the assignment of errors which is filed herewith, and prays that this appeal be allowed and that citation issue as provided by law, and that a transcript of the record, proceed-
[fol. 70] ings and papers upon which said judgment was based, duly authenticated, may be sent to the United States Circuit Court of Appeals for the Fifth Circuit, as by the rules in said Court in such cases made and provided.

Appellant further shows that this appeal is prosecuted under the direction and authority of the Attorney General of the United States of America, and therefore prays that said appeal may be allowed without bond.

Lawrence S. Camp, United States Attorney for the Northern District of Georgia. M. Neil Andrews, Assistant United States Attorney for the Northern District of Georgia.

IN UNITED STATES DISTRICT COURT

ORDER GRANTING APPEAL—Filed August 14, 1935

The foregoing petition considered, the appeal is allowed as prayed and the appeal, being prosecuted by direction of the Attorney General of the United States, it is ordered that the same be allowed without bond being given by the appellant.

It is further ordered that a supersedeas be granted, and pending a determination of this appeal, the judgment of the Court as of April 11, 1935, and the same is superseded.

This 10th, day of August, 1935.

Wm. H. Barrett, United States Judge Designate.

[fol. 71] IN UNITED STATES DISTRICT COURT

ASSIGNMENT OF ERRORS—Filed August 14, 1935

Comes now, on this 9th day of August, 1935, the Defendant, J. T. Rose, former Collector of Internal Revenue, by his attorneys, Lawrence S. Camp, United States Attorney, and M. Neil Andrews, Assistant United States Attorney, and, in connection with his petition for appeal, files the following assignment of errors, upon which he will rely upon the prosecution of appeal from the judgment of this Court entered herein on the 11th day of April, 1935:

1

The Court erred in granting and allowing Plaintiff's motion for a directed verdict in favor of Plaintiff upon the grounds that under the law applied to the pleadings, the stipulation of facts, and the other evidence in the case, as a matter of law, such a verdict was demanded, which motion was made at the conclusion of all the evidence in the case, to which ruling of the Court Defendant then and there excepted and the exception was duly allowed by the Court.

2

The Court erred in granting and allowing the Plaintiff's motion for judgment upon the verdict theretofore made by the jury by direction of the Court and the signing and entering a judgment in favor of the Plaintiff for the amounts in said judgment set forth and to the granting of which motion and the signing and entering of which judgment the Defendant then and there excepted, and the Defendants' exceptions were duly allowed by the Court.

[fol. 72]

3

The Court erred in granting and allowing a certificate of probable cause, based upon the verdict and judgment theretofore rendered on the 11th day of April, 1935, in favor of the Plaintiff and against the Defendant, to which granting and allowance of said certificate of probable cause the Defendant then and there excepted, and his exceptions were duly allowed.

4

The Court erred in overruling and denying the Defendant's motion for a directed verdict in favor of the Defendant upon the grounds: (a) "That the pleadings of the evidence are legally insufficient to support any judgment in favor of the Plaintiff in the cause," and (b) "That under the pleadings and the evidence the Plaintiff is estopped to assert the claim that any portion of the taxes in controversy in this action were not taxable to the estate of S. C. McEachern," which motion was made at the conclusion of all the evidence in the case, to which ruling of the Court Defendant then and there excepted, and his exception was duly allowed by the Court.

5

The Court erred in admitting in evidence over objections of the Defendant, paragraphs 1 and 2 of the stipulation of facts offered by the Plaintiff, designated "Plaintiff's Exhibit 4," filed as part of the record in said cause, to which ruling of the Court the Defendant then excepted and an exception was duly allowed.

6

The Court erred in sustaining the Plaintiff's objection to the introduction of Defendant's stipulation marked "Defendant's Exhibit A" in evidence, on the ground that the facts covered by the stipulation were irrelevant in [fol. 73] that they undertook to support a defense of estoppel, and even though the stipulation were admitted, estoppel would not be established, and in excluding the Defendant's said stipulation from the evidence, to which ruling of the Court the Defendant then excepted and his exception was duly allowed.

Wherefore, the Defendant prays that the judgment of the Court upon the verdict be set aside and a new trial be granted.

Lawrence S. Camp, United States Attorney for the Northern District of Georgia. M. Neil Andrews, Assistant United States Attorney for the Northern District of Georgia.

IN UNITED STATES DISTRICT COURT

PRÆCIPE—Filed August 28, 1935

To the Clerk of the Above-entitled Court:

You will please prepare a transcript of the record in this cause to be filed in the office of the clerk of the United States Circuit Court of Appeals for the Fifth Judicial Circuit, under the appeal heretofore perfected to said Court, and include in said transcript the following pleadings, proceedings and papers on file, to-wit:

1. Petition.
2. Answer.
3. Defendant's Motion for Directed Verdict.

[fol. 74] 4. Verdict and Judgment.

5. Bill of Exceptions.
6. Petition for Appeal.
7. Order granting Appeal.
8. Assignments of Error.
9. Præcipe.
10. Citation.
11. Clerk's certificate.

Lawrence S. Camp, United States Attorney; M. Neil Andrews, Assistant United States Attorney, Attorneys for Appellant.

Service of a copy of this præcipe acknowledged.
This 28th day of August, 1935.

Sutherland, Tuttle & Brennan, Attorneys for Appellee.

[fol. 75] Original citation omitted from the printed record, the original thereof being on file in the office of the Clerk of the United States Circuit Court of Appeals.

[fol. 76] That thereafter the following proceedings were had in said cause in the United States Circuit Court of Appeals for the Fifth Circuit, viz:

ARGUMENT AND SUBMISSION

Extract from the Minutes of October 6, 1936

No. 7911

J. T. ROSE, Former Collector of Internal Revenue for the District of Georgia,

versus

D. W. McEACHERN, Administrator of the Estate of S. C. McEachern, Deceased

On this day this cause was called, and, after argument by Edward P. Hodges, Esq., Special Assistant to the Attorney General, for appellant, and W. A. Sutherland, Esq., for appellee, was submitted to the Court.

[fol. 77] OPINION OF THE COURT—Filed November 9, 1936

IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 7911

J. T. ROSE, Former Collector of Internal Revenue for the District of Georgia, Appellant,

versus

D. W. McEACHERN, Administrator of the Estate of S. C. McEachern, Deceased, Appellee

Appeal from the District Court of the United States for the Northern District of Georgia

(November 9, 1936)

Before Sibley, Hutcheson, and Holmes, Circuit Judges

HUTCHESON, Circuit Judge:

The suit was to recover as overpayments taxes paid in 1929, 1930 and 1931. They were paid by appellee as ad-

ministrator of the estate of S. C. McEachern on account of collections of certain installment obligations held by the deceased at his death. Appellant, admitting that the amounts sued for had been in form erroneously paid, defended against paying them back on the ground that those amounts and more were due by plaintiff to the United States on ac- [fol. 78] count of those obligations, and that therefore "under the circumstances of the case, he was not obligated by the ties of natural justice and equity to refund the money."

In support of this position, he pointed out by answer and stipulation, that under Sec. 44(d) of the Revenue Act of 1928, the transmission by death of the unpaid installments should have been returned for the period from January 1, 1928 to December 12, 1928, and a tax of $11,625, an amount greatly in excess of the amount sued for, paid on account thereof. He insists that having failed to make such return, and having instead made incorrect and misleading returns as upon sales for each of those years, plaintiff may not now, limitation having barred the collection of the larger sum due the United States, get back the smaller sums paid on his incorrect returns.

The District Judge thought that these matters did not constitute an estoppel or otherwise operate to defeat the suit. He excluded the stipulation regarding them as irrelevant. The cause then standing solely on the stipulation that the sums sued for had been erroneously collected as taxes, he directed a verdict for plaintiff.

Appellant is here complaining of the overruling of his motion for a direction, of the direction of verdict for plaintiff, and of the ruling of the court excluding the stipulation. These are the facts as stipulated.

On September 3, 1924, S. C. McEachern the decedent, by a purchase contract sold 500 shares of the capital stock of the Industrial Life & Health Insurance Company for the sum of $300,000, $30,000 to be paid in cash, the balance in quarterly installments of $7,500 each, payable on March 1, 1925 and on the first day of each and every third month thereafter. The stock had cost him $10 a share, or $5000. [fol. 79] On December 12, 1928, with installments aggregating $150,000 still unpaid, he died intestate. On February 4, 1929 appellee was granted letters testamentary and qualified as administrator. For the years 1929, 30 and 31 he filed

estate income tax returns, reporting in each year as income, amounts equal to the profits on the installments collected in it, based on the original cost of the stock to decedent, and paid taxes accordingly. The returns, however, did not show these profits as derived from collections on installment obligations. Each showed a complete sale in that year of 50 shares. Plaintiff has made no return of the gain or profit received from the transmission of the installments. The only reference he ever made to these installments was in the Federal estate tax rturn to list among the assets of the estate, "unpaid balances of deferred payments on 250 shares of stock of the Industrial Life & Health Insurance Company under contract of S. C. McEachern to J. N. McEachern, as trustee, dated September 3, 1924, value $125,000." This value of $125,000 had been arrived at by discounting the face value of the $150,000 of future installment payments approximately 6.35% per annum from McEachern's death to the average due date of the installments.

Appellant insisted below and insists here, that appellee having based his returns upon a misstatement of fact, and having paid his taxes upon that misstatement, is now, limitation having run, estopped to correct it by showing that he did not sell 50 shares in each of those years as he reported he had done, but merely in each year collected some of the deferred instalment obligations. He cites in support cases holding that a taxpayer having asserted the existence of a state of facts and paid his taxes on that basis, though incorrect, may not thereafter, when limitation has run against collection on the correct basis, unsay what he has said to recover back the sums he has paid. Shamrock Oil Co. vs. Commr., 77 Fed. (2d) 555; Hartwell Mills vs. [fol. 80] Rose, 61 Fed. (2d) 441; Wheelock vs. Commr., 77 Fed. (2nd) 474; Swartz vs. Commr., 69 Fed. (2d) 633; Adler vs. Commr., 77 Fed. (2d) 733; Bothwell vs. Commr., 77 Fed. (2d) 35; Larkin vs. United States, 78 Fed. (2d) 951; Crane vs. Commr., 68 Fed. (2d) 640; Askin & Marine Co. vs. Commr., 66 Fed. (2d) 776; Stearns vs. United States, 291 U. S. 54.

He argues, too, that when the nature of the action plaintiff has brought is considered, it must be plain that plaintiff cannot recover in it. For to do so he must show not merely that defendant has obtained money from plaintiff

by one or another device which he was not entitled to employ, but that regardless of the method of its obtaining he withholds money from plaintiff which ex aequo et bono he may not justly withhold. J. W. Carter Music Co. vs. Bass, 20 Fed. (2d) 390; Champ Spring Co. vs. United States, 47 Fed. (2d) 1; Hartwell Mills vs. Rose, 61 Fed. (2d) 441; Lewis vs. Reynolds, 284 U. S. 281; Bull vs. United States, 295 U. S. 247.

Appellee replies that every element of estoppel is lacking here; that appellee did not misstate any fact with reference to the particular taxes collected, which has or could have misled any one. He argues further that from the statement in the estate tax return showing the installment obligations as assets of the estate, the Commissioner was charged with knowledge and did in fact know, that the administrator was under a mistake of law erroneously carrying forward the practice of the decedent in returning as income, gains on the installments as received. Finally, he argues that Sec. 44 (d) of the 1928 Act, the statute appellant invokes, is without force as unconstitutional.

We take up the last point first. No court which has [fol. 81] examined the statute has yet thought it unconstitutional.[1] We do not think it is. We regard as unsubstantial the difference appellee seeks to draw between the case of a sale made before and one made after the passage of the Act. It is true that in some of the cases notably Crane vs. Helvering, 76 Fed. (2d) 99, which dealt with installment sales made after the statute took effect, some piont is made of the volition of the seller in adopting the installment basis with knowledge of the existence of the statute. We agree, however with the views expressed in Lawler vs. Commr., 78 Fed. (2d) 567 and Moore vs. United States, 10 Fed. Supp. 143, that the time of the sale whether before or after the passage, is without substantial bearing on the validity of the Act.

We come then, to consider appellee's case as it really stands, the case of one who, though on a correct basis should

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Note 1: Crane vs. Helvering, 76 Fed. (2d) 99; Nuckolls vs. U. S., 76 Fed. (2d) 357; Lawler vs. Commr. 78 Fed. (2d) 567; Williams vs. Commr., 79 Fed. (2d) 518; Provident Trust Co. of Philadelphia vs. Commr., 76 Fed. (2d) 810; Moore vs. United States, 10 Fed. Supp. 143.

have paid considerably more as taxes on account of these installment obligations than he has paid on an incorrect basis, cannot, because of the course he has taken, limitation having now run, be made to pay on the correct basis. So considering it, we think it perfectly plain that though the sums he paid were paid on a particular theory of obligation which did not exist, he may not recover these sums back because they are in sum less than the amount which on a correct theory of obligation, he ought to have paid on account of these installment obligations. This is so not because of the existence of a technical estoppel or a waiver, but because his action was equitable in its nature and grounds, and he may not succeed in it unless he can show that the defendant has money which, ex aequo et bono, the defendant ought to refund.

[fol. 82] In Moses vs. McFarlane, 2 Burroughs, 1005, where the statement of the principle was first clearly announced, it is said:

"If the defendant be under an obligation from the ties of natural justice to refund, the law imposes a debt and gives an action founded on the equity of plaintiff's case, as it were, upon a contract quasi ex contractu, as the Roman law expresses it. This kind of equitable action to recover back money which ought not in justice to have been paid is very beneficial and therefore much encouraged. It lies only for money which ex aequo et bono the defendant ought to refund. It does not lie for money paid by plaintiff which is claimed of him as payable on a point of honor or honesty although it could not have been recovered from him through any course of law, as in the payment of a debt barred by the statute of limitation, or contracted during infancy, or to the extent of principal and legal interest upon a usurious contract, or for money lost at play, because in all these cases the defendant may defend with a safe conscience, though by positive law he is barred from recovery. In other words, the gist of this kind of action is that the defendant, under the circumstances of the case, is obliged by the ties of natural justice and equity to refund the money."

While generally appropriate in efforts to get back money which is being wrongfully withheld, it is peculiarly appropriate in actions in fact between the taxpayer and the Government, though the suit is in form against the collector. Moore Ice Cream Co. vs. Rose, 289 U. S. 373. Sometimes

in these actions the inability to recover the money is spoken of as springing from estoppel; sometimes it is put on the more general ground of the inequities of the case. Grounded [fol. 83] in repugnance against unjust enrichment, the action is given wide and liberal application in all cases where money is wrongfully withheld. It may not be used to obtain money which the plaintiff ought not in good conscience, to have back.[2]

The judgment is reversed and the cause remanded for further and not inconsistent proceedings.

[fol. 84] JUDGMENT

Extract from the Minutes of November 9th, 1936

No. 7911

J. T. ROSE, Former Collector of Internal Revenue for the District of Georgia,

versus

D. W. McEACHERN, Administrator of the Estate of S. C. McEachern, Deceased

This cause came on to be heard on the transcript of the record from the District Court of the United States for the Northern District of Georgia, and was argued by counsel;

On consideration whereof, It is now here ordered and adjudged by this Court, that the judgment of the said District Court in this cause be, and the same is hereby, reversed; and that this cause be, and it is hereby, remanded to the said District Court for further and not inconsistent proceedings.

Note 2: c/f United States vs. Jefferson Electric Co., 291 U. S. 386; United States Paper Co. vs. Bowers, 80 Fed. (2d) 82; Myers vs. Hurley, 273 U. S. 27; Richardson Lubricating Co. vs. Kinney, 168 N. E. 886; Perry vs. United States, 294 U. S. 330.

[fol. 85] MOTION AND ORDER STAYING MANDATE—Filed November 21, 1936

IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 7911

J. T. ROSE, Former Collector of Internal Revenue, Appellant,

v.

D. W. McEACHERN, Administrator of the Estate of S. C. McEachern, Deceased, Appellee

Motion to Stay Issuance of Mandate

Now Comes D. W. McEachern, Administrator of the Estate of S. C. McEachern, deceased, appellee in the above entitled cause, and shows to this court that he intends to apply to the Supreme Court of the United States for a writ of certiorari to review the judgment rendered by this court, and that he intends to make said application within three (3) months after the decision of this court on November 9, 1936.

Wherefore, appellee prays that the mandate of this court be stayed and withheld until February 9, 1937, or in the event that a petition for writ of certiorari is filed and docketed in the Supreme Court prior to the expiration of said time, then until final disposition of the cause in the Supreme Court.

This 18th day of November, 1936.

(Signed) W. A. Sutherland, Joseph B. Brennan, Attorneys for Appellee.

[fol. 86] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH DISTRICT

No. 7911

J. T. ROSE, Former Collector of Internal Revenue for the District of Georgia, Appellant,

versus

D. W. McEACHERN, Administrator of the Estate of S. C. McEachern, Deceased, Appellee

On Consideration of the Application of the Appellee in the above numbered and entitled cause for a stay of the

mandate of this court therein, to enable Appellee to apply for and to obtain a writ of certiorari from the Supreme Court of the United States, it is Ordered that the issue of the mandate of this court in said cause be and the same is stayed for a period of thirty days; the stay to continue in force until the final disposition of the case by the Supreme Court, provided that within thirty days from the date of this order there shall be filed with the clerk of this court the certificate of the clerk of the Supreme Court that the certiorari petition, and record have been filed, and that due proof of service of notice thereof under Paragraph 3 of Rule 38 of the Supreme Court has been given. It is further ordered that the clerk shall issue the mandate upon the filing of a copy of an order of the Supreme Court denying the writ, or upon the expiration of thirty days from the date of this order, unless the above-mentioned certificate shall be filed with the clerk of this court within that time.

Done at New Orleans, La., this 21st day of November, 1936.

(Signed) Rufus E. Foster, United States Circuit Judge.

[fol. 87] Motion and Order for Additional Stay of Mandate—Filed December 17, 1936

In the United States Circuit Court of Appeals for the Fifth Circuit

No. 7911

J. T. Rose, Former Collector of Internal Revenue, Appellant,

v.

D. W. McEachern, Administrator of the Estate of S. C. McEachern, Deceased, Appellee

Motion to Stay Issuance of Mandate

Now Comes D. W. McEachern, Administrator of the Estate of S. C. McEachern, deceased, appellee in the above entitled cause, and shows to this court that he intends to apply to the Supreme Court of the United States for a writ of certiorari to review the judgment rendered by this court on November 9, 1936, and appellee further shows that on

November 21, 1936, this court entered an order staying the issuance of its mandate for a period of thirty (30) days from November 21, 1936, and appellee further shows that additional time will be required to prepare a petition for certiorari and supporting brief.

Wherefore, appellee prays that the mandate of this court be further stayed and withheld until January 20, 1937, or in the event that a petition for writ of certiorari is filed and docketed in the Supreme Court prior to the expiration of [fol. 88] said time, then until the final disposition of the cause in the Supreme Court.

This 16th day of December, 1936.

(Signed) W. A. Sutherland, Joseph B. Brennan, Attorneys for Appellee.

[fol. 89] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH DISTRICT

No. 7911

J. T. ROSE, Former Collector of Internal Revenue for the District of Georgia, Appellant,

versus

D. W. McEACHERN, Administrator of the Estate of S. C. McEachern, Deceased, Appellee.

On Consideration of the Application of the Appellee in the above numbered and entitled cause for a further stay of the mandate of this court therein, to enable Appellee to apply for and to obtain a writ of certiorari from the Supreme Court of the United States, it is Ordered that the issue of the mandate of this court in said cause be and the same is further stayed for a period of thirty days; from December 21, 1936; the stay to continue in force until the final disposition of the case by the Supreme Court, provided that within thirty days from December 21, 1936 there shall be filed with the clerk of this court the certificate of the clerk of the Supreme Court that the certiorari petition and record have been filed, and that due proof of service of notice thereof under Paragraph 3 of Rule 38 of the Supreme Court has been given. It is further ordered that the clerk shall issue the mandate upon the filing of a copy of an order of the Supreme Court denying the writ, or upon the

expiration of thirty days from December 21, 1936, unless the above-mentioned certificate shall be filed with the clerk of this court within that time.

Done at New Orleans, La., this 17th day of December, 1936.

(Signed) J. C. Hutcheson, Jr., United States Circuit Judge.

[fol. 90] CLERK'S CERTIFICATE

UNITED STATES OF AMERICA:

UNITED STATES CIRCUIT COURT OF APPEALS, FIFTH CIRCUIT

I, Oakley F. Dodd, Clerk of the United States Circuit Court of Appeals for the Fifth Circuit, do hereby certify that the pages numbered from 76 to 89 next preceding this certificate contain full, true and complete copies of all the pleadings, record entries and proceedings, including the opinion of the United States Circuit Court of Appeals for the Fifth Circuit, in a certain cause in said Court, numbered 7911, wherein J. T. Rose, former Collector of Internal Revenue for the District of Georgia, is appellant, and D. W. McEachern, Administrator of the Estate of S. C. McEachern, deceased, is appellee, as full, true and complete as the originals of the same now remain in my office.

I further certify that the pages of the printed record numbered from 1 to 75 are identical with the printed record upon which said cause was heard and decided in the said Circuit Court of Appeals.

In testimony whereof, I hereunto subscribe my name and affix the seal of the said United States Circuit Court of Appeals, at my office in the City of New Orleans, Louisiana, in the Fifth Circuit, this 12th day of January, A. D. 1937.

Oakley F. Dodd, Clerk of the United States Circuit Court of Appeals, Fifth Circuit. (Seal United States Circuit Court of Appeals, Fifth Circuit.)

[fol. 91] SUPREME COURT OF THE UNITED STATES, OCTOBER TERM, 1936

No. —

D. W. McEACHERN, Administrator of the Estate of S. C. McEachern, Deceased, Petitioner,

v.

J. T. ROSE, Former Collector of Internal Revenue

ORDER EXTENDING TIME WITHIN WHICH TO APPLY FOR WRIT OF CERTIORARI

On consideration of the application of counsel for Petitioner in the above-entitled cause, and good cause therefor having been shown, it is now herein ordered that the time within which a petition for a writ of certiorari may be filed herein be and the same is hereby extended to and including February 24, 1937.

This 1st day of February, 1937.

Benjamin N. Cardozo, Associate Justice of the Supreme Court of the United States.

[fol. 92] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed April 5, 1937

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Fifth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: Enter W. A. Sutherland. File No. 41,290. U. S. Circuit Court of Appeals, Fifth Circuit. Term No. 6. D. W. McEachern, Administrator of the Estate of S. C. McEachern, Deceased, petitioner, vs. J. T. Rose, Former Collector of Internal Revenue for the District of Georgia. Petition for a writ of certiorari and exhibit thereto. Filed February 23, 1937. Term No. 6, O. T., 1937.

FILE COPY

Office - Supreme Court, U. S.
FEB 23 1937
CHARLES ELMORE CROPLEY
CLERK

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936.

No. [redacted] 6

D. W. McEACHERN, ADMINISTRATOR OF THE ESTATE OF S. C. McEACHERN, DECEASED,

Petitioner,

vs.

J. T. ROSE, FORMER COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

W. A. SUTHERLAND,
Counsel for Petitioner.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936.

No. 750

D. W. McEACHERN, Administrator of the Estate of S. C. McEachern, Deceased,

Petitioner,

vs.

J. T. ROSE, Former Collector of Internal Revenue for the District of Georgia.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

Petition.

D. W. McEachern, Administrator of the estate of S. C. McEachern, deceased, by his counsel, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Fifth Circuit, entered in the above case on November 9, 1936 (R. 81), reversing the judgment of the United States District Court for the Northern District of Georgia.

Summary Statement of Matter Involved.

The petitioner, as administrator of the estate of S. C. McEachern, deceased, brought this suit seeking recovery

of amounts by which McEachern's estate overpaid its Federal income taxes for the years 1929, 1930 and 1931 (R. 1-18). The respondent for defense asserted that petitioner was estopped from recovering such overpayments by reason of the fact that a larger amount of income tax due for the year 1928 remained unpaid, collection of the 1928 tax being barred by the statute of limitations (R. 19-30). The overpayments of tax for 1929, 1930 and 1931, and the alleged underpayment of tax for 1928 arose as follows:

In 1924 the petitioner's intestate, hereinafter called the "decedent," sold 500 shares of stock in the Industrial Life & Health Insurance Company for a total consideration of $300,000.00, payable $30,000.00 in cash at the time of said sale, and the balance in quarterly installments of $7,500.00 each (R. 3, 19).

As permitted by law, the decedent elected, in returning his profit from the sale for Federal income tax, to return such profit on the installment basis (R. 20). The decedent died on December 12, 1929, at which time $150,000.00 of the purchase price remained unpaid (R. 4, 19).

In 1929, 1930 and 1931 the decedent's estate collected a part of the aforesaid installment obligations of $150,000.00 which had remained unpaid at decedent's death (R. 3, 8, 13, 19, 22, 25). It is not disputed that such collections constituted income to the decedent's estate only to the extent that such collections exceeded the value of the installment obligations at the date of decedent's death, this result following from the fact that upon decedent's death such installment obligations became capital assets in the hands of the decedent's estate at their then value. However, in the returns filed for the decedent's estate for 1929, 1930 and 1931 (R. 33-50) the petitioner erroneously continued to report the income from such collections on the same basis on which the decedent would have been required to report the same if he had continued to live, and as a result the

petitioner erroneously reported for 1929, 1930 and 1931 an excessive amount of income from such collections. The excessive income thus reported resulted in the overpayments of tax for 1929, 1930 and 1931, which are sought to be recovered in this suit (R. 1-18). The amount of recovery to which the petitioner is entitled is not in dispute, the only issue being whether or not the petitioner is estopped from any recovery at all.

The alleged underpayment of tax for 1928 arises under Section 44(d) of the 1928 Revenue Act. Section 44(d) was new in the 1928 Revenue Act and the prior Revenue Acts contained no similar provisions. Under Section 44(d) the passing or transmission of the $150,000.00 of unpaid installment obligations from the decedent to his estate was declared to result in the accrual of income to the decedent in the year of his death in an amount equal to the profit which the decedent would have realized if he had sold such installment obligations on the date of his death for their then market value. Such alleged income thus deemed to accrue to the decedent under Section 44(d) was not reported in the income tax return filed for the decedent for 1928. Prior to the 1928 Revenue Act it was not taxed as income to anyone.

The petitioner contended in the courts below, and still contends that, as applied to the facts of this case, Section 44(d) of the 1928 Revenue Act is unconstitutional under Article 1, Section 2 of the Constitution, and is not authorized by the Sixteenth Amendment to the Constitution, in that Section 44(d) seeks to tax the decedent upon income which he never realized.[1] If Section 44(d) is unconstitutional, then there is no underpayment of tax for 1928.

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[1] Section 44(d) attempts to tax whatever appreciation took place in the value of the $150,000.00 of non-interest bearing installment obligations between the date of their receipt in 1924 and the date of decedent's death in 1928. On no possible theory was this appreciation ever income to the decedent within the meaning of the Sixteenth Amendment.

The respondent contended that Section 44(d) was constitutional; that the decedent's income tax for 1928 was therefore underpaid; and that such underpayment for 1928 furnished the basis for an estoppel against petitioner with respect to the overpayments sought to be recovered for 1929, 1930 and 1931.

The petitioner contended further that, even assuming Section 44(d) was constitutional, there was still no basis for estoppel, because, among other reasons, the Commissioner of Internal Revenue had timely knowledge of all of the material facts with reference to the alleged underpayment of tax for 1928, and simply overlooked their legal significance, so that his failure to collect the alleged tax for 1928 was in no way due to his having been misled by the petitioner. In support of this contention, the petitioner proved that on December 12, 1929, the petitioner filed a Federal estate tax return for the decedent's estate, which estate tax return disclosed the existence of the unpaid installment obligations in question, and disclosed that such obligations passed and were transmitted upon the death of the decedent, to his estate (R. 51, 52). The passing or transmission of these installment obligations from the decedent to his estate was the event which brought into operation the provisions of Section 44(d), under which the alleged tax liability for 1928 arose. The statute of limitations upon the collection of additional tax for 1928 did not expire until approximately fifteen months after the estate tax return was filed. The estate tax return was investigated with usual care and the Field Agent's Report thereon was made and transmitted to the Bureau of Internal Revenue in Washington on May 31, 1930 (R. 65), at which time the statute of limitations on collection of additional income tax for 1928 had still over nine months to run.

The respondent admitted that all of the mistakes made by the petitioner were innocent mistakes of law, and that

the petitioner at all times acted in good faith (R. 65, 66). *The respondent did not even seek to introduce any evidence to show that the Commissioner's failure to collect the alleged tax for 1928 was due to his having been misled by the petitioner.*

The District Court, holding that there was no estoppel, in any event, and that it was therefore unnecessary to pass upon the constitutionality of Section 44(d), directed a verdict and entered judgment in favor of the petitioner (R. 31, 32). The Circuit Court of Appeals reversed the judgment of the District Court and held, first, that Section 44(d) is constitutional, and, second, that because of the barred tax liability for 1928, the petitioner is not entitled to recover the admitted overpayments for 1929, 1930 and 1931 (R. 76-81). The Circuit Court of Appeals stated in its opinion that "Sometimes in these actions the inability to recover the money is spoken of as springing from estoppel; sometimes it is put on the more general ground of the inequities of the case" (R. 80, 81).

Reasons for Granting the Writ.

1. The decision of the Circuit Court of Appeals in the case at bar is in conflict, on the question of estoppel, with the decision of this Court in *Helvering* v. *Salvage,* 297 U. S. 106, and with the decision of the Circuit Court of Appeals for the Second Circuit in the same case, reported as *Salvage* v. *Commissioner,* 76 F. (2d) 112; and is also in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *Commissioner* v. *Union Pacific R. Co.,* 86 F. (2d) 637; and is also in conflict with the decision of the Circuit Court of Appeals for the Fourth Circuit in *A. G. Hull* v. *Commissioner,* — F. (2d) —, decided January 5, 1937, published in 1937 Commerce Clearing House Federal Tax Service, Paragraph 9035.

2. The question of the possible scope and extent of estoppel in Federal income tax cases is a question on which, as is shown in the brief in support hereof, the Circuit Courts of Appeals have adopted widely divergent views, and is an important question of Federal law which is involved in a large and constantly increasing number of cases. Great confusion already exists, and greater confusion seems likely to arise, if the fundamental question involved is not settled by this Court.

3. As is shown in the brief in support hereof, the decision of the Circuit Court of Appeals in the case at bar is substantially similar, on the question of estoppel, to the decision of the Circuit Court of Appeals for the Tenth Circuit in the case of *Commissioner* v. *Farren*, 82 F. (2d) 141. This Court granted a petition for certiorari in the *Farren* case, *supra*, on June 1, 1936 (Nos. 973 and 974, October Term, 1935; Nos. 43 and 44, October Term, 1936), but the proceedings in this Court in the *Farren* case were dismissed upon stipulation of the parties thereto on October 26, 1936.[2] It is respectfully submitted that the same reasons which justified the granting of the petition for certiorari in the *Farren* case, *supra*, are present in the case at bar and justify the granting of this petition.

WHEREFORE it is respectfully prayed that the petition be granted.

W. A. SUTHERLAND,
Counsel for Petitioner.

February, 1937.

[2] The circumstances in connection with the dismissal of the *Farren* case, after this Court had granted certiorari to the taxpayer, over the opposition of the Solicitor General, and after the taxpayer had filed his brief on the merits, seem significant. According to our information, the Government initiated the settlement of the case, and in order to effect the settlement and secure the dismissal of the case, the Government gave up approximately 75% of the amount in dispute, all of which it would have been entitled to retain if the lower court's holding of estoppel had been upheld by this Court.

BRIEF IN SUPPORT OF PETITION.

Opinions Below.

There was no opinion by the District Court. The opinion of the Circuit Court of Appeals is reported at 86 F. (2d) 231 and will be found at page 76 of the record.

Jurisdiction.

The judgment of the Circuit Court of Appeals sought to be reviewed was entered on November 9, 1936 (R. 81). On February 1, 1937, Honorable Benjamin N. Cardozo entered an order of this Court extending the time for filing a petition for certiorari in the case at bar to and including February 24, 1937. Jurisdiction to issue the writ requested is found in the provisions of Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Statement of the Case, Statutes Involved.

A statement of the case will be found in the petition. The statutes involved appear in the appendix.

Specifications of Error.

The Circuit Court of Appeals erred:

1. In holding that the Petitioner is estopped, by reason of the alleged barred tax liability for 1928, from recovering the overpayments of taxes for 1929, 1930 and 1931.

2. In holding that on equitable principles springing from estoppel, the petitioner is precluded, by reason of the alleged barred tax liability for 1928, from recovering the overpayments of taxes for 1929, 1930 and 1931.

3. In holding that the petitioner is not entitled *ex aequo et bono* and in good conscience to recover the overpayments of taxes for 1929, 1930 and 1931.

4. In holding that Section 44(d) of the Revenue Act of 1928 is constitutional, and in failing to hold that such section is unconstitutional under Article 1, Section 2 of the Constitution and is not authorized under the Sixteenth Amendment to the Constitution, in that it seeks to tax the decedent upon income which he never realized.

5. In failing to hold that for the following reasons there is no estoppel in the case at bar:

(a) The Commissioner of Internal Revenue was timely advised of all the material facts in connection with the alleged barred tax for 1928, and the Commissioner's failure to collect the alleged tax for 1928 was therefore not due to his having been misled by the petitioner.

(b) The petitioner's failure to report the alleged omitted income for 1928 was due solely to an innocent mistake of law.

(c) The petitioner does not seek in this suit to change any position previously taken by it, which position has resulted, or will result, in any loss of revenue to which the Government was entitled.

(d) Section 44(d) of the Revenue Act of 1928 is unconstitutional and there is therefore no underpayment of tax for 1928 and no injury to the Government to constitute the basis of an estoppel.

6. In failing to hold that the substantive provisions of the statutes of limitation and the statutory policy of taxing income in the year when it is received render invalid the respondent's defense based on the alleged barred tax liability for 1928, in the absence of estoppel.

7. In failing to hold that the petitioner was entitled to recover the overpayments of taxes for 1929, 1930 and 1931.

8. In reversing the judgment of the District Court.

ARGUMENT.

I. The decision in the case at bar is in conflict with the decisions of the Circuit Courts of Appeals for the Second Circuit and the Fourth Circuit.

In *Salvage* v. *Commissioner*, 76 F. (2d) 112 (C. C. A. 2d), the taxpayer made a bargain purchase of stock in 1922, under such circumstances that he received income in 1922 in an amount equal to the difference between the purchase price paid by him for the stock and the value of the stock when received by him. The taxpayer failed to report in 1922 the income which he thus received. In determining his capital gain on the subsequent sale of the stock in 1929, the taxpayer sought to use the correct capital base, namely, the value of the stock at the time when received by him in 1922. The statute of limitations had run on the collection of additional tax for 1922. The Commissioner relied on estoppel. The Circuit Court of Appeals for the Second Circuit held that the capital base claimed by the taxpayer was correct; that the failure to disclose the 1922 income apparently resulted from an innocent mistake of law; that there was no false representation of fact; and that nothing gave support to the claim of estoppel. This Court affirmed in *Helvering* v. *Salvage*, 297 U. S. 106, holding that the defense of estoppel was not properly raised and should have been passed by the court below, and holding also that "Furthermore, the facts disclosed give it no support".

In *Commissioner* v. *Union Pacific R. Co.*, 86 F. (2d) 637 (C. C. A. 2d), the taxpayer had sold property at a profit in 1917 and 1920. Through mistake the taxpayer reported the profit from such sales as income for 1926, whereas such

profit should have been reported as income in 1917 and 1920. After the statute of limitations had barred the collection of additional tax for 1917 and 1920, the taxpayer sought to have its tax liability for 1926 determined upon a correct basis, by eliminating from its income for 1926 the profit which should properly have been reported for 1917 and 1920. The Commissioner relied upon estoppel: The Circuit Court of Appeals for the Second Circuit held that the person claiming the benefit of estoppel must have been ignorant of the true facts and must have been adversely affected by the acts of the person against whom the estoppel is claimed; that the Commissioner had timely knowledge of all of the material facts, and that therefore there was no estoppel. The Court stated further:

> "An unqualified application of the rule that failure to report income creates estoppel would mean that an equitable remedy can serve to nullify the substantive provisions of the statute of limitations as well as the statutory policy that income is to be allocated to its appropriate year, Burnet *v.* Sanford & Brooks Co., 282 U. S. 359, 51 S. Ct. 150, 75 L. ed. 383, despite the loss of revenue, Helvering *v.* St. Louis S. W. Ry. Co., 66 F. (2d) 633 (C. C. A. 8)."

In *A. G. Hull* v. *Commissioner* (C. C. A. 4th, Jan. 5, 1937), — F. (2d) —, published in 1937 Commerce Clearing House Federal Tax Service, Paragraph 9035, the taxpayer received $100,000.00 as consideration for his grant of an option to purchase property owned by him. The Commissioner sought to treat the sum so received as income of the taxpayer for 1926. The taxpayer denied that the receipt of such sum constituted income to him at any time, but contended in the alternative that it was income to him in 1925 if at all. The taxpayer had not reported such sum as income in either 1925 or 1926. The statute of limitations had run on the collection of additional tax for 1925 and the

Commissioner relied on estoppel. The Circuit Court of Appeals for the Fourth Circuit held that if the amount in question was income at any time, it was income in 1925 and not in 1926; and held further that there was no estoppel, since the Commissioner had full knowledge of all the material facts long before the statute of limitations expired.

In both the *Salvage* case, *supra,* and the *Union Pacific R. Co.* case, *supra,* the Circuit Court of Appeals for the Second Circuit cited and relied upon *Sugar Creek Coal & Mining Co.*, 31 B. T. A. 344. In the *Sugar Creek* case, as in the *Salvage* and *Union Pacific R. Co.* cases, *supra,* there was a barred tax claim against the taxpayer for prior years resulting from the taxpayer's failure to report income in such prior years. The Commissioner claimed that the taxpayer was estopped from seeking a correct adjustment of his taxes for a later year. The Board of Tax Appeals held that since the Commissioner had timely knowledge of all of the material facts and was not misled to his prejudice by the taxpayer, there was no estoppel. The Board said, with reference to the Commissioner's attempt to assert the defense of estoppel under such circumstances:

> "This proposition would operate as a complete frustration of the statute of limitations. Congress having expressly provided such a bar, the Commissioner would thrust it aside whenever it seemed to him or to the Board or the courts unfair, although there is in the act neither express nor implied exception of such a nature. This is also true of refunds of overpayments, for the Commissioner may not act merely upon his sense of fairness to allow a claim long after it is outlawed by statutory limitation. In the absence of fraud or at least of conscious deception, Congress has fixed a period of time as a limit upon collectibility, and this may not give way to an elusive concept of fairness.
>
> "There may be a tinge of unfairness in the thought that a taxpayer may, because of the statutory limita-

> tion, avoid a tax otherwise unquestionably due. But, on the other hand, it may be unfair that an honest taxpayer should be made to answer for an innocent mistake long afterward. These matters Congress has considered and in its legislative wisdom it has enacted the limitation period at the price of losing the tax. The administrative officer may not interpose his judgment to the contrary, Dupree *v.* Mansur, 214 U. S. 161."

The view taken by the Circuit Courts of Appeals for the Second Circuit and Fourth Circuit and by the Board of Tax Appeals, in the cases cited above, is recommended in concise terms in a recent text by the present Undersecretary of the Treasury as follows:

> "If the taxpayer is to be estopped, the usually accepted analysis requires that he shall have made some representation of fact; that the Commissioner shall have relied upon it; and shall have changed his position to his detriment. In some cases these three elements can be shown, *but the courts should be more insistent than they have been upon actual proof on each point, as distinguished from vague assertions of unfairness by counsel for the Treasury.*"[1] (Italics supplied.)

In the case at bar, the Circuit Court of Appeals, on similar facts, took the conflicting view and relied upon the vague ground of unfairness rather than upon proof of the recognized elements of estoppel. The petitioner contended that there was no estoppel in the case at bar because, among other reasons, the Commissioner had timely knowledge of all of the material facts and was therefore not misled to his prejudice by the petitioner. The Circuit Court of Appeals apparently recognized this fact, for it stated that the petitioner's inability to recover is based not on a "technical estoppel", but on broad equitable principles "spring-

[1] Roswell Magill, Taxable Income (1936), pp. 164, 165.

ing from estoppel'' (R. 80, 81). The Circuit Court of Appeals held that the petitioner was not entitled *''ex æquo et bono''* (R. 80) or ''in good conscience'' (R. 81) to the relief sought, which of course is merely equivalent to holding that petitioner's claim is ''unfair''.

As stated above, the Circuit Court of Appeals for the Second Circuit and the Fourth Circuit, in the cases cited above, insisted upon proof of the recognized elements of estoppel, as distinguished from vague assertions of unfairness by the Government attorneys. In the case at bar the Circuit Court of Appeals on similar facts failed to require proof of the recognized elements of estoppel and instead rested its decision on the vague ground of unfairness. The decision in the case at bar is therefore clearly in conflict with the decisions of the Circuit Court of Appeals for the Second Circuit in the *Salvage* and *Union Pacific R. Co.* cases, *supra,* and with the decision of the Circuit Court of Appeals for the Fourth Circuit in the *Hull* case, *supra.*

II. The Farren Case.

In *Union Pacific R. C., supra,* the Circuit Court of Appeals for the Second Circuit expressly recognized the conflict with *Commissioner* v. *Farren,* 82 F. (2d) 141 (C. C. A. 10th).

In the *Farren* case, *supra,* the taxpayer received stock in 1918 as compensation for services. Under an innocent mistake of law, the taxpayer failed to report the income which he thus received in 1918. In determining his gain upon the subsequent sale of the stock in 1926, he sought to use the correct capital base, namely, the value of the stock when received by him in 1918. The statute of limitations barred the collection of additional tax for 1918, and the Commissioner relied upon estoppel. The Circuit Court of Appeals for the Tenth Circuit sustained the Commissioner's defense, on general grounds of unfairness, relying principally

upon language used by this Court in *Stearns* v. *United States,* 291 U. S. 54, to the effect that "no one shall be permitted to found any claim upon his own inequity, * * * "[2]

In the *Farren* case, as in the *Salvage* case, *supra,* there was no estoppel, because the failure to report income in the prior year was due solely to an innocent mistake of law, and there was no misrepresentation of fact. In its decision in the *Farren* case, the Circuit Court of Appeals for the Tenth Circuit recognized the conflict with the *Salvage* case, but considered that it was not bound by this Court's decision in the *Salvage* case, since this Court's decision in the *Salvage* case was rested in part on a procedural point.

The decisions of the Circuit Courts of Appeals in the case at bar and in the *Farren* case are substantially similar, as is shown by the following:

(a) The facts in the two cases were similar in that in each case the taxpayer sought a correct adjustment of his tax liability for a later year, and in each case there was alleged to be a barred claim against the taxpayer for additional taxes for a prior year.

(b) In each case the defense relied upon was estoppel.

(c) In neither case were the recognized elements of estoppel proven.

(d) In each case the Court rested its decision ultimately upon the vague ground of unfairness, and failed to require proof of the recognized elements of estoppel.

The two courts identified their respective decisions to the same extent with the doctrine of estoppel, the court saying in the case at bar: "Sometimes in these actions the inability to recover the money is spoken of as springing from estoppel,

[2] *Stearns* v. *United States, supra,* involved a clear case of estoppel by conduct, and therefore, when read in the light of its facts, does not support the conclusion reached in the *Farren* case.

* * *" (R. 80, 81); while in the *Farren* case, the court there said: "Sometimes the resulting disability has been characterized as an estoppel, * * *."

It follows that the same questions are involved in the case at bar as in the *Farren* case; that the case at bar, equally with the *Farren* case, is in conflict with the *Union Pacific R. Co.* case, *supra;*[3] and that the case at bar will bring before this Court for review the same questions which were before this Court in the *Farren* case. The questions involved in this case would undoubtedly have been settled by this Court in its decision in the *Farren* case, had not that case been dismissed in this Court by the parties.

III. Importance of Question Involved.

The question of the proper scope of the doctrine of estoppel in income tax cases, as presented by the clear conflict between the Circuit Courts of Appeals above referred to, is a question of vital importance in the administration of the income tax laws. The Bureau of Internal Revenue and the Department of Justice are constantly seeking to rely upon so-called "estoppel" in every conceivable type of situation, regardless of whether one or more of the elements of equitable estoppel, as generally understood, are absent.[4]

---

[3] As stated above the Circuit Court of Appeals for the Second Circuit, in *Union Pacific R. Co., supra,* expressly recognized the conflict with the *Farren* case.

[4] Maguire and Zimet, "Hobson's Choice and Similar Practices in Federal Taxation", 48 Harvard Law Review 1281, at p. 1294, state: "The term estoppel is now constantly on the lips of Bureau employees, but with such vague and shifting significance as to bewilder any serious thinker."

Paul & Mertens, Law of Federal Income Taxation, 1936 Supp., Sec. 53.13, state: "Estoppel does not seem to have been strenuously pressed by government attorneys until about 1929, and at first the plea did not meet with conspicuous success. However, the doctrine of estoppel, notwithstanding some earlier Government reverses, soon became firmly imbedded in tax law. As will be noted from the discussion below, the Government now resorts to the defense on every possible occasion."

Equitable estoppel, as applied to cases other than income tax cases, is a doctrine which has been developed by the courts over a period of many years. Its limits are well defined. The elements necessary to constitute an equitable estoppel may be summarized as follows: (a) misrepresentation of fact by the party sought to be estopped; (b) reliance thereon by the other party in ignorance of the true facts; and (c) action thereon by such other party to his prejudice. In cases other than income tax cases, the application of equitable estoppel within the recognized limits as just described, is recognized as being sufficient to protect against unfairness in the assertion of legal rights.

However, the doctrine of estoppel, as Government attorneys have sought to apply it with increasing frequency in income tax cases, has no relation whatever in scope to true estoppel as defined above. Sometimes in the attempt to extend the doctrine beyond its proper scope, the designation of "estoppel" or "equitable estoppel" is retained; sometimes the attempted defense is called "quasi-estoppel"; sometimes it is asserted to rest upon "broad equitable principles based on estoppel". In the case at bar, the Respondent in his pleadings and throughout the entire case has constantly described his defense simply as "estoppel" (R. 22, 25, 29, 31, 67). The Circuit Court of Appeals rested its decision in the case at bar upon so-called broad equitable principles "springing from estoppel" (R. 81). Whatever the designation used, it is clear that in every case the attempted extension of estoppel is based ultimately upon *vague assertions of unfairness.*

The logical application of the decision of the court below, in the case at bar, would largely wipe out the defense of the statute of limitations in income tax cases, as was stated to this Court in the *Farren* petition for certiorari. The question is therefore of such importance, in such a large number

of cases, that it should challenge the attention of this Court, even if there were no conflict. However, it has been shown above that a clear conflict does exist, the Circuit Courts of Appeals for the Second and Fourth Circuits having indicated that such *vague assertions of unfairness* as are here relied upon were not enough, and having insisted upon proof of the recognized elements of estoppel; while in the case at bar and in the *Farren* case, the Circuit Courts of Appeals for the Fifth and Tenth Circuits have adopted the conflicting view.

Under the circumstances, to avoid great and growing confusion, the desirability of an early decision by this Court, resolving this conflict, seems apparent.

Conclusion.

The question involved in this case is an important question of Federal law, on which the decisions of the Circuit Courts of Appeals are in conflict, and it is therefore respectfully submitted that this petition for certiorari should be granted, and the conflict resolved.

Respectfully submitted,

W. A. SUTHERLAND,
Counsel for Petitioner.

APPENDIX.

Section 44(d), Revenue Act of 1928.

"Gain or loss upon disposition of installment obligations.—If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and (1) in the case of satisfaction at other than face value or a sale or exchange—the amount realized, or (2) in case of a distribution, transmission, or disposition otherwise than by sale or exchange—the fair market value of the obligation at the time of such distribution, transmission, or disposition. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full."

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. [redacted] 6

D. W. McEACHERN, ADMINISTRATOR OF THE ESTATE OF S. C. McEACHERN, DECEASED,

Petitioner,

vs.

J. T. ROSE, FORMER COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA.

On Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit.

REPLY MEMORANDUM FOR PETITIONER.

W. A. SUTHERLAND,
Counsel for Petitioner.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 750.

D. W. McEACHERN, ADMINISTRATOR OF THE ESTATE OF S. C. McEACHERN, DECEASED,

Petitioner,

vs.

J. T. ROSE, FORMER COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA.

On Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit.

REPLY MEMORANDUM FOR PETITIONER.

In opposing the granting of certiorari in this case, the Respondent argues that the decision of the Circuit Court of Appeals does not rest on estoppel, but on recoupment, and that there is therefore no conflict of decisions as stated in the petition for certiorari herein.

As was pointed out in the brief in support of the petition (pp. 14, 15), the decisions in the case at bar and in *Commissioner* v. *Farren*, 82 F. (2d) 141, both rest upon similar *vague grounds of unfairness*, coupled in some hazy way with the doctrine of estoppel. In the case at bar, the Circuit Court of Appeals identified its decision with the doctrine of estoppel to *exactly the same extent* as did the Court in the *Farren* case. A comparison of the opinion of the court below with the opinion in the *Farren* case makes this readily apparent.

It follows therefore that if the *Farren* case is in conflict with *Salvage* v. *Commissioner*, 76 F. (2d) 112, *Commissioner* v. *Union Pacific R. Co.*, 86 F. (2d) 637, and *A. G. Hull* v. *Commissioner*, 87 F. (2d) 260, then the case at bar is equally in conflict with those decisions. The conflict of the *Farren* case with the case of *Commissioner* v. *Union Pacific R. Co., supra*, was expressly recognized by the Circuit Court of Appeals for the Second Circuit in the latter case. The nature of the conflict is fully described in the brief in support of petition at pages 12-17.

It follows therefore that the Respondent errs in denying that the decision of the Circuit Court of Appeals in the case at bar is in conflict with *Salvage* v. *Commissioner*, *Commissioner* v. *Union Pacific R. Co.*, and *A. G. Hull* v. *Commissioner, supra.*

In connection with the Respondent's suggestion that the decision of the Circuit Court of Appeals in the case at bar rests on recoupment, it may be observed that the opinion nowhere refers to recoupment or otherwise indicates that the court below relied on the doctrine of recoupment. But even if the decision did rest on recoupment, it would be clear that this Court should grant the petition for certiorari, because in that event this case would present the same questions which are before this Court in *Stone* v. *White*, No. 202, October Term, 1935, and in *United States ex rel Girard Trust Co.* v. *Helvering*, No. 285, October Term,

1936, in which cases this Court has granted certiorari since the petition for certiorari was filed in the case at bar.

It is therefore prayed that the petition be granted.

Respectfully submitted,

W. A. SUTHERLAND,
Counsel for Petitioner.

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Supreme Court of the United States.

OCTOBER TERM, 1937.

No. 6.

D. W. McEACHERN, Administrator of the Estate of S. C. McEACHERN, Deceased,

PETITIONER,

v.

J. T. ROSE, Former Collector of Internal Revenue for the District of Georgia.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

BRIEF FOR PETITIONER.

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Supreme Court of the United States.

OCTOBER TERM, 1937.

No. 6.

D. W. McEACHERN, Administrator of the Estate of S. C. McEACHERN, Deceased,

PETITIONER,

v.

J. T. ROSE, Former Collector of Internal Revenue for the District of Georgia.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

BRIEF FOR PETITIONER.

OPINION BELOW.

There was no opinion by the District Court. The opinion of the Circuit Court of Appeals is reported at 86 F. (2d) 231, and will be found at page 57 of the Record.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered on November 9, 1936 (R. 62). On February 1, 1937, the Honorable Benjamin N. Cardozo entered an order of this Court extending the time for filing a petition for certiorari in the case at bar to and including February 24, 1937 (R. 67). The petition for a writ of certiorari was filed February 23, 1937, and was granted April 5, 1937 (R. 67). The jurisdiction of this Court rests on Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED.

Whether petitioner is precluded, by reason of an alleged barred income tax liability for 1928, from recovering overpayments of income taxes for 1929, 1930 and 1931; and whether Section 44(d) of the Revenue Act of 1928, under which the alleged barred income tax liability for 1928 arises, is constitutional as applied in this case.

STATUTES INVOLVED.

The statutes involved are set forth in Appendix A.

STATEMENT.

The petitioner, as administrator of the estate of S. C. McEachern, deceased, brought this suit seeking recovery of amounts by which McEachern's estate overpaid its Federal income taxes for the years 1929, 1930 and 1931 (R. 1-13). The respondent did not deny that such taxes had

been overpaid, but asserted for defense that petitioner was estopped from recovering such overpayments by reason of the fact that certain income tax due for the year 1928 in an amount not specified remained unpaid, collection of the 1928 tax being barred by the statute of limitations (R. 15-24). The overpayments of tax for 1929, 1930 and 1931, and the alleged underpayment of tax for 1928, arose as follows:

In 1924 the petitioner's intestate, hereinafter called the "decedent," sold 500 shares of stock in the Industrial Life & Health Insurance Company for a total consideration of $300,000.00, payable $30,000.00 in cash at the time of said sale, and the balance in quarterly installments of $7,500.00 each (R. 3, 15).

As permitted by law, the decedent elected, in returning his profit from the sale for Federal income tax, to return such profit on the installment basis. The decedent died on December 12, 1928, at which time $150,000.00 of the purchase price remained unpaid (R. 3, 15).

In 1929, 1930 and 1931 the decedent's estate collected a part of the aforesaid installment obligations of $150,000.00, which had remained unpaid at decedent's death (R. 3, 15; 6, 18; 11, 21). It is not disputed that such collections constituted income to the decedent's estate only to the extent that such collections exceeded the value of the installment obligations at the date of decedent's death, this result following from the fact that upon decedent's death such installment obligations became capital assets in the hands of the decedent's estate at their then value. However, in the returns filed for the decedent's estate for 1929, 1930 and 1931 (R. 29, 33, 36), the petitioner erroneously reported the income from such collections on the same basis on which the decedent would have been required to

report the same if he had continued to live, and as a result the petitioner erroneously reported for 1929, 1930 and 1931 an excessive amount of income. The excessive income thus reported resulted in the overpayments of tax for 1929, 1930 and 1931, which are sought to be recovered in this suit (R. 1-13). The amount of recovery to which the petitioner is entitled is not in dispute, the only issue being whether or not the petitioner is precluded, by reason of the alleged barred tax liability for 1928, from any recovery at all.

The alleged barred tax liability for 1928 arises under Section 44(d) of the 1928 Revenue Act, set forth in the Appendix. Under Section 44(d), as construed by the Commissioner, the passing or transmission of the $150,000.00 of unpaid installment obligations from the decedent to his estate was declared to result in the receipt of income by the decedent in the year of his death. Such alleged income under Section 44(d) was not reported in the income tax return filed for the decedent for 1928.

It was admitted that the 1928 income tax return and all other returns filed by the petitioner were filed in good faith (R. 50).

The respondent contended that the petitioner was estopped, by reason of the alleged barred tax liability for 1928, from recovering the overpayments for 1929, 1930 and 1931. The only evidence which respondent offered with respect to the alleged tax for 1928 was a stipulation designated as Defendant's Exhibit A (R. 46-49), which stipulation was excluded by the trial court on the ground that the facts covered by the stipulation were irrelevant in that they undertook to establish the defense of estoppel, and even though the stipulation were admitted, estoppel would not be established (R. 55).

In answer to such contention, the petitioner contended

that there was no tax liability for 1928 for the reason that Section 44(d), under which the alleged tax for 1928 arises, is unconstitutional as applied in this case.

The petitioner contended further that, even assuming Section 44(d) was constitutional, there was still no basis for estoppel, because, among other reasons, the Commissioner of Internal Revenue had timely knowledge of all the material facts with reference to the alleged underpayment of tax for 1928, and his failure to collect the alleged tax for 1928 was in no way due to his having been misled by the petitioner. In support of this contention, the petitioner proved that on December 12, 1929, the petitioner filed a Federal estate tax return for the decedent's estate, which estate tax return disclosed the existence of the unpaid installment obligations in question, and disclosed that such obligations passed and were transmitted, upon the death of the decedent, to his estate (R. 39). The passing or transmission of these installment obligations from the decedent to his estate was the event which gave rise, under Section 44(d), to the alleged tax liability for 1928. The statute of limitations upon the collection of additional tax for 1928 did not expire until approximately fifteen months after the estate tax return was filed.[1] The estate tax return was investigated with usual care, and the Field Agent's Report thereon was made and transmitted to the Bureau of Internal Revenue in Washington on May 31, 1930 (R. 50), at which time the statute of limitations on collection of additional tax for 1928 had still over nine months to run.

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[1] The 1928 income return was filed March 12, 1929 (R. 46). Therefore the two year statute of limitations under Section 275 of the 1928 Revenue Act did not expire until March 12, 1931. The estate tax return was filed 15 months prior thereto, namely, on December 12, 1929 (R. 39).

The District Court directed a verdict and entered judgment in favor of the petitioner (R. 25, 54), holding that there was no estoppel and that it was therefore unnecessary to pass upon the constitutionality of Section 44(d). The Circuit Court of Appeals reversed the judgment of the District Court and held: (1) that Section 44(d) is constitutional, and (2) that because of the barred tax liability for 1928, the petitioner is not entitled to recover the overpayments for 1929, 1930 and 1931 (R. 57-62).

SPECIFICATION OF ERRORS.

The Circuit Court of Appeals erred:

(1) In holding that Section 44(d) of the Revenue Act of 1928 is constitutional, and in failing to hold that such section is unconstitutional under Article I, Section 2 of the Constitution and is not authorized under the Sixteenth Amendment to the Constitution, as applied in this case.

(2) In holding that the petitioner is estopped or otherwise precluded, by reason of the alleged barred tax liability for 1928, from recovering the overpayments of tax for 1929, 1930 and 1931.

(3) In failing to hold that the petitioner was entitled to recover the overpayments of taxes for 1929, 1930 and 1931.

(4) In reversing the judgment of the District Court.

SUMMARY OF ARGUMENT.

The respondent's entire defense rests upon the assertion of the alleged barred tax for 1928. The petitioner contends that there is no barred tax for 1928, for the reason that Section 44(d) of the 1928 Revenue Act, under which

such alleged tax for 1928 arises, is unconstitutional as applied in this case. Section 44(d) as applied in this case attempts to tax the decedent upon a "gain" declared to result from the transmission of property by death. Such an event cannot give rise to income within the meaning of the Sixteenth Amendment.

The petitioner contends further that even if Section 44(d) is constitutional, and even if there is therefore a barred tax for 1928, such barred tax for 1928 does not preclude the petitioner from recovering the overpayments for 1929, 1930 and 1931.

The petitioner urges first that there is no estoppel, for the reason that the person claiming the benefit of estoppel must have been ignorant of the true facts and must have been adversely affected by the acts of the person against whom the estoppel is claimed; whereas in the case at bar, the Commissioner had timely knowledge of all the material facts, as disclosed by the petitioner in the decedent's estate tax return, and was in no way misled by the petitioner with respect to the facts giving rise to the alleged tax for 1928.

The petitioner next contends that the issue of recoupment is not open for consideration in this case. A plea of recoupment must allege the existence of a claim, must state the amount of the claim, and must pray that such claim be set up to reduce or wipe out the main cause of action. None of these three essentials is found in any pleading filed by the respondent. The petitioner therefore contends that the issue of recoupment is not open.

The petitioner urges further that there are no special equities in this case which permit the respondent to defend on the ground of the alleged barred tax for 1928. It is well established that the Government may not defeat a

suit for refund of taxes simply by asserting a barred tax claim for a prior year, in the absence of equitable circumstances which in some way connect the barred tax with the refund sought in such manner as to render the refund claim inequitable. Such equitable circumstances most commonly arise in cases wherein the taxpayer has taken a certain position resulting in nonpayment of the barred tax, and has later sought to change that position by taking an inconsistent position after the statute of limitations has expired, with resulting loss to the Government of the barred tax. In the case at bar, petitioner is not seeking to undo or change any position which resulted in loss of revenue to the Government, and is not seeking to take any inconsistent position whatsoever with reference to the alleged barred tax for 1928. The petitioner seeks only to correct the error made by petitioner in overpaying its income taxes for 1929, 1930 and 1931, and that error had absolutely no connection with the Government's failure to collect the alleged barred tax for 1928. Furthermore, the facts were all timely disclosed to the Government in the estate tax return; the Government's failure to collect the alleged tax for 1928 is not excusable on the ground of adverse court decisions or otherwise, and the overpayments here sought to be recovered were, with the exception of $230.07, all paid after the statute of limitations barred collection of the alleged tax for 1928. There are therefore no special equities in this case which will permit the respondent to establish a defense based on the alleged barred tax for 1928, and such defense is nothing more than an attempt to offset the alleged tax for 1928 against the petitioner's right to a refund of the totally unrelated overpayments for 1929, 1930 and 1931. This Court has held that such offset will not be permitted.

ARGUMENT.

I.

SECTION 44(d) IS UNCONSTITUTIONAL AS APPLIED IN THE PRESENT CASE.

An essential element in the defense which the Circuit Court of Appeals upheld in this action, is an alleged income tax liability which is asserted against petitioner's intestate under Section 44(d) of the Revenue Act of 1928. Respondent contends that a tax under that section was imposed on decedent, but never paid, with respect to the transmission of certain "installment obligations" by death. Petitioner contends that Section 44(d) as applied in such a case is unconstitutional, in that it attempts to tax something which is not income under the Sixteenth Amendment. It is indisputable that if Section 44(d) is unconstitutional, respondent's defense falls. On the other hand, if Section 44(d) is valid and applicable, petitioner contends that the defense is without merit for reasons developed in the latter part of this brief.

In so far as it may pertain to the present case, Section 44(d) provides as follows:

> "If an installment obligation is * * * transmitted * * * gain or loss shall result to the extent of the difference between the basis of the obligation and * * * the fair market value of the obligation at the time of such transmission * * *. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full."

As that section has been construed by the Commissioner

(I. T. 2515, IX-1 C. B. 125), Congress has attempted by ipse dixit to make gain result to the decedent from the transmission of certain property to his Administrator by reason of death. Under that ruling,

> "The gain or loss resulting from the transmission • • • should be included in the decedent's return for the taxable year in which his death occurred."

It must be too plain for words that a decedent cannot realize *income* in any sense of the term by reason of the transfer of his property to others as a result of his death. The section is clearly invalid as attempting to tax as income something that is not income under the Sixteenth Amendment. *Eisner v. Macomber,* 252 U. S. 189.

Such a bold attempt to distort the concept of income cannot be matched, except perhaps by the attempt of a New York State Comptroller to tax the "income" resulting to a donor by reason of a gift of property that had increased in value in his hands. *People v. Wendell,* 196 App. Div. 613, 188 N. Y. Supp. 510. The idea was of course repudiated by the court, which pointed out the absurdity of attributing a gain to the donor by reason of the fact that he had given away the property and thus had lost it in toto.

Apart from Section 44(d), the limit to which the Federal Government has gone in attempting to predicate a realization of gain upon the disposition of property otherwise than by a sale, exchange or similar transaction, was reached in the case of *General Utilities & Operating Co. v. Helvering,* 296 U. S. 200. In that case the Government contended in this court that a corporation might realize gain by the distribution of property to its stockholders as a dividend in kind, where the property had increased in value in the hands of the corporation. See respondent's

brief in No. 41, October Term, 1935, pp. 13-28. In making this contention the Government recognized that Treasury officials and the congressional committees had expressed doubt as to the constitutionality of a provision requiring such a result. See brief cited, p. 18n. See also Hearings before House Ways & Means Committee on Revenue Revision, 1934, p. 150. However, the Government's argument in that case was based upon the theory that the dividend distribution under the circumstances satisfied a general legal obligation which the corporation owed to its stockholders, and no suggestion was made that income could be realized by a donor by an outright gift of property. See brief cited, pp. 22, 25.

Any further discussion of the invalidity of Section 44(d) should be unnecessary. But we anticipate that the Government will attempt to support Section 44(d) on the theory that its effect is to tax something other than what it says should be taxed. The lower Federal Courts which have upheld the section in cases like the present[2] seem to have proceeded on the assumption that Section 44(d) simply taxes the untaxed portion of a profit that could have been taxed in full in the year of the sale.[3] It will be shown that such an assumption is clearly unfounded and that Section 44(d) cannot be justified upon any such principle.

In order to make a fair presentation of the theory of the lower court cases just cited, and to show that the theory

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[2] Moore v. United States, 10 F. Supp. 143 (Ct. Cls.); Provident Trust Co. of Philadelphia v. Commissioner, 76 F. (2d) 810 (C. C. A. 3rd); Williams v. Commissioner, 79 F. (2d) 518 (C. C. A. 3rd); Lawler v. Commissioner, 78 F. (2d) 567 (C. C. A. 9th).

[3] Even if Section 44(d) could be construed as doing this, it would impose a new tax in 1928 with respect to a sale in 1924. Under such circumstances, the tax should clearly be held unreasonably retroactive, and therefore contrary to the due process clause of the Fifth Amendment. Cf. United States v. Hudson, 299 U. S. 498.

cannot be sustained, it will be well to discuss briefly the installment sales provisions in general, and the legislative history and purpose of Section 44(d).

Beginning with the Revenue Act of 1926, which was given retroactive application,[4] Congress has provided that the installment sales method of reporting the profit on a sale of property involving deferred payments may be employed at the election of the seller, where the initial payment does not exceed a certain percentage of the entire purchase price.[5] By electing that method the seller would report in each taxable year "that proportion of the installment payments actually received in that year which the total profit realized or to be realized when the payment is completed, bears to the total contract price."

Section 44(d) was written into the law in 1928 as a means of compensating for a loss of tax revenue resulting from the use, in certain circumstances, of the installment method of reporting income. Where a seller used the installment method of reporting a gain from the sale of property in his return for the year of the sale, he would show as income for that year only the proportionate part of the cash payments actually received in the year which represented gain. If, in the next year, before the receipt of any further payments, he should make a gift of the installment obligations, or if he should die, there was no provision of law prior to the 1928 Act under which he could be taxed on any part of the profit other than the proportionate part returned in the first year.

In many cases the profit actually taxed, under the in-

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[4] See Sections 212(d) and 1208 of the Revenue Act of 1926, quoted in Appendix A, infra.

[5] The percentage was 25% under Section 212(d) of the 1926 Act, 40% under Section 44(b) of the 1928 Act, and 30% under Section 44(b) of the 1934 Act.

stallment method, prior to the gift of the installment obligations, or their transmission by death, would be substantially less than the profit which could have been taxed in the year of the sale if the installment method had not been available. It was to compensate for the loss, in such circumstances, of a tax which could have been imposed in the year of sale, that Section 44(d) was enacted.[6]

However, it will be apparent from an analysis of the provisions that *Section 44(d) does NOT simply tax the untaxed balance of a profit which could have been taxed in its entirety in the year of the sale.* This should be clear from a consideration of the fact that the fair market value of installment obligations at the death of the seller, which is an essential element in a computation under Section 44(d), can have no place whatever in the measure of a profit realized by the seller upon the sale in some prior year.

The profit actually realized in the year of sale, and which could be taxed in that year, may be greater or may be less than the profit reported on the installment basis during the life of a seller who dies prior to the final payment of the purchase price. It would be mere chance or coincidence in any case if the "gain" taxable under Section 44(d) turned out to be the untaxed balance of the gain from the original sale that could have been taxed in prior years.

The amount of profit which could be taxed in its entirety in the year of a sale involving deferred payments would depend upon the nature and value of the purchase money obligations. If the deferred payments are represented by negotiable promissory notes which have a fair market

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[6] See House Rep. No. 2, 70th Cong., 1st Sess., p. 16; Senate Rep. No. 960, 70th Cong., 1st Sess., p. 24.

value, and are the equivalent of cash to that extent, the seller realizes by the sale a profit measured by the excess of cash and fair market value of notes over the cost of the property sold. If the notes bear a reasonable rate of interest, and if they are adequately secured, their fair market value at the time of sale may equal their face amount. In such a case Congress could constitutionally tax in the year of the sale the entire profit to be realized from the transaction, with the exception of the interest payable on the purchase money notes, which would be taxable as received.

On the other hand, if the purchase money notes have a fair market value at the time of sale, of only 50% of their face amount, Congress cannot constitutionally tax the seller with the entire profit to be realized from the transaction until the notes are actually collected. If the seller reports on the installment basis in such a case and dies before the collection of all deferred payments, the profits taxed to him during life may actually exceed the profit that could have been taxed as having been realized at the time of sale, plus the profits resulting from collections as made.[7]

In a case like the present, where the deferred payments were not represented by notes or other specialties, and did not bear interest, the correct method of reporting gain on the sale, in the absence of the installment sales method, would probably be to treat the collections first as a return of the seller's capital or cost and any excess as income. G. C. M. 1387, VI-1 C. B. 48. And cf. *Burnet v. Logan*, 283 U. S. 404. In such a case, if the seller dies before the final payment, the amount taxable on the installment basis will be greater than the amount that could be taxed under

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[7] For a graphic illustration of this possibility, see Appendix B, infra.

the method approved in the General Counsel's Memorandum just cited.[8]

It is thus apparent that where a seller, who has reported on the installment period, dies prior to the final payment of the purchase price, there may or there may not be an untaxed balance of a profit which could have been taxed to the seller under some other method. *If Congress had wanted simply to collect the balance of a tax which it could have collected in some prior year, but did not, it could have expressed this purpose in so many words.* It could have provided that:

> Where installment obligations are distributed or transmitted, otherwise than by sale or exchange, and where it appears that the seller had elected to report the sale on the installment method, there should be taxed to the seller in the year of such distribution or transmission that portion of the profit actually realized upon the sale which had not been previously taxed under the installment method.

But Section 44 (d) does not attempt to do this.

As applied here, Section 44 (d) would impose a tax on the decedent with respect to a fictitious "gain" measured by the excess of the fair market value of the purchase money obligations at the seller's death over the "basis" of the obligations. "Basis" is defined as "the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obliga-

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[8] If this method were applied here, a profit of only $145,000.00 would have been taxed to decedent upon the collection of $150,000.00 during life, the entire cost of $5000.00 being applied against first collections. On the other hand, a profit of $147,500.00 was taxable to decedent under the installment method, without giving any consideration to Section 44(d).

tion satisfied in full." The definition is periphrastic, but the effect of the section is to tax in the year of death the profit that would have been realized if the obligation were collected in full, with a certain adjustment based upon the market value of the obligation at the time of the seller's death. If the market value of the obligation at the seller's death is less than the face amount, the profit that would have been realized upon the eventual collection in full should be reduced to the extent of the deficiency in market value, in order to arrive at the "adjusted profit" taxable under Section 44 (d).

It must be apparent from the foregoing that the "profit" which Section 44 (d) attempts to tax has no relation to the profit which could have been taxed in the year of sale. The profit realized by the decedent on the sale in 1924 depended in part upon the fair market value of the purchase money obligations *at that time*, if they had any such value. Whatever value the uncollected obligations had in 1928, when decedent died, has nothing to do with the gain realized in 1924.

Viewing Section 44 (d) in another light, it has the effect of taxing the unrealized appreciation in the value of the installment obligations between the date of sale and the date of death, in addition to the gain realized upon the sale. It may be granted that a seller, on a cash receipts and disbursements basis, realizes taxable gain measured by the excess of cash and market value of purchase money obligations at the time of sale over the cost of the property sold. But in the computation of "gain" under Section 44 (d) it is not the value of these obligations at the time of sale, but their value at the date of death which is controlling. The effect of Section 44 (d) is thus to tax any appreciation in the value of these obligations between

sale and death, although such appreciation is never realized.

The Circuit Court of Appeals for the Second Circuit has recognized that in so far as Section 44 (d) attempts to tax this unrealized appreciation in value, it is aimed at something which is not income under the Sixteenth Amendment. *Crane v. Helvering,* 76 F. (2d) 99. In that case Section 44 (d) was sustained as applied to a sale *after* the passage of the 1928 Act, upon a theory which will be presently discussed. However, Circuit Judge Learned Hand, writing the opinion of the court, clearly recognized that Section 44 (d) undertakes to tax something which is not income in such a case. Judge Hand said:

> "The (purchase money) debt, though secured by the property sold, may be of less value than its face when received; usually it is. If so, it is likely to increase between its receipt by the testator and his death, and section 44 (d) taxes that increase, though it is not 'realized.' Under Eisner v. Macomber, 252 U. S. 189, such an increase is not income and is beyond the power of Congress under the Sixteenth Amendment."

But notwithstanding the clear recognition of the fact that such increase in value could not be taxed as income under the Sixteenth Amendment, Section 44 (d) was there upheld as applied to a sale in 1929, which the seller elected to report on the installment method authorized by Section 44 (b) of the 1928 Act. The basis for the decision is expressed in the following language from Judge Hand's opinion:

> "The statute might have taxed at once, a gain based upon the value of the bond and mortgage, for that was 'realized' as soon as they were received * * *. Sec-

> tion 44 (b) gave the taxpayer a privilege to avoid such a tax if he wished, but affixed to it the condition that if he died, the value of the obligation should be regarded as then realized."

A similar result was reached by the Circuit Court of Appeals for the Tenth Circuit in *Nuckolls v. United States*, 76 F. (2d) 357. The Court there said:

> "Congress is not required by the constitution to extend the privilege (of reporting on the installment basis) at all, as indeed it did not prior to 1926; when it did so, it had a right to attach thereto this condition. The taxpayer is not obliged to avail himself of the privilege conferred; if he does so, he takes it with the condition attached."

The decisions in the two cases just cited are justified on the principle that Congress can tax some things that are not income, where the treatment of such items is voluntarily accepted by the taxpayer as a condition to the exercise of a privilege which Congress need not extend. Compare *Helvering v. Independent Life Insurance Co.*, 292 U. S. 371. In that case this Court recognized that the rental value of space occupied by an insurance company in its own building could not constitutionally be taxed as income under the Sixteenth Amendment, but it was held that the treatment of such an item as income could be voluntarily accepted by the taxpayer as a condition to the allowance of certain deductions which were a matter of legislative grace.

However, similar principles cannot possibly be applied in a case like the present one. Here the sale occurred in 1924, and Section 44(d) was not enacted until 1928. There was nothing in the law like Section 44(d) prior to its en-

actment. Before the 1928 Act it was clear that an installment seller could not be taxed upon the disposition of installment obligations either by gift, or by death.[10]

Petitioner cannot possibly be in the position of one who has voluntarily agreed to be taxed with respect to something that is not income, as a condition of the exercise of a privilege.

As construed by the Commissioner, Section 44(d) attempts to impose an income tax on a decedent with respect to a so-called "gain" resulting from the transmission of certain property by death. No gain within the meaning of the Sixteenth Amendment can possibly result from any such transaction, and Section 44(d) is therefore invalid. As applied in a case like the present, where the original sale was made before the enactment of Section 44(d), the Section cannot be sustained on any other theory.

II.

THERE IS NO ESTOPPEL SINCE THE COMMISSIONER HAD TIMELY KNOWLEDGE OF THE MATERIAL FACTS GIVING RISE TO THE ALLEGED TAX FOR 1928, AND WAS IN NO WAY MISLED BY THE PETITIONER WITH RESPECT THERETO.

Under Heading I above it has been shown that there is no tax due for 1928 for the reason that Section 44(d) of the 1928 Revenue Act, under which the alleged tax for 1928 arises, is unconstitutional as applied to the facts of this case. Under this Heading II and the remaining portions of this brief, it will be shown that even if Section 44(d) is constitutional, and even if there is therefore a barred tax

[10] See note 6, supra.

liability for 1928, as alleged by the respondent, such barred tax liability for 1928 does not establish any defense for the respondent in this suit. Under this Heading II it will be shown that there is no estoppel.

It is well established that the person claiming the benefit of an estoppel must have been ignorant of the true facts and must have been adversely affected by the acts of the person against whom the estoppel is claimed. It follows that there is no estoppel in this case because: (1) The material facts giving rise to the alleged tax for 1928 were all fully disclosed to the Commissioner in the estate tax return filed by the petitioner long before the statute of limitations ran on the collection of such alleged tax for 1928; and (2) the petitioner made no misrepresentations which could possibly have caused the Commissioner's failure to collect the alleged tax for 1928.

The material facts giving rise to the alleged tax for 1928 under Section 44(d) are the existence of the installment obligations in question and the passing or transmission of those installment obligations from the decedent to his estate upon the decedent's death. *These very facts which give rise to the alleged tax for 1928, namely, the existence of the installment obligations in question and the passing or transmission of those installment obligations from the decedent to his estate, were affirmatively disclosed by the petitioner in the decedent's estate tax return filed approximately 15 months before the statute of limitations ran on collection of the alleged tax for 1928* (R. 39).[11] Since the petitioner thus affirmatively disclosed all of the material facts to the Commissioner long before the statute of limitations ran on 1928, it is plain that the Commissioner's

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[11] See footnote 1 at page 5, supra.

failure to collect the alleged tax for 1928 was in no way the result of his having been misled by the petitioner.

It appears further that at no time did the petitioner make any misrepresentation which could possibly have caused the Commissioner's failure to collect the alleged tax for 1928. Acting under a mistake which the respondent admits was made innocently and in good faith (R. 50), the petitioner, in making the income tax returns for the decedent's estate for 1929, 1930 and 1931, erroneously reported a sale of 50 shares of the stock in question in each year (R. 41, 43, 44), whereas the petitioner should have reported in each year the collection of an installment on the purchase price of 500 shares of stock sold in 1924. However, the erroneous representation that 50 shares of stock were sold in each year could not possibly have led the Commissioner to reach the totally unrelated conclusion that the decedent owned no installment obligations at his death, and therefore such erroneous representation could not possibly have caused the Commissioner's failure to collect the alleged tax for 1928.

It may be pointed out further that the petitioner's erroneous treatment of these installment collections appears quite plainly on the face of the 1929, 1930 and 1931 returns as a mistake. For example, the 1929 return stated on its face that the 50 shares of stock were acquired in 1918 (R. 29); and at the same time showed on its face that the taxpayer making the return was the estate of a decedent who had died on December 12, 1928 (R. 26). The most casual investigation of this 1929 return would necessarily have disclosed the fact that some mistake had been made, since an estate which only came into existence on December 12, 1928, could not have acquired 50 shares of stock in 1918. Had the Commissioner made any effort to correct this ob-

vious error in the 1929 return, such effort would undoubtedly have led to a timely collection of the alleged tax for 1928 under Section 44(d). It is interesting to note that this error which appeared so plainly on the face of the 1929 return was obviously an error against the taxpayer's interest, which may or may not have had anything to do with the Commissioner's failure to correct it.[12]

The rule that a person claiming the benefit of an estoppel must have been ignorant of the true facts and must have been adversely affected by the acts of the person against whom the estoppel is claimed is applicable in Federal income tax cases as well as in other fields. See *Commissioner v. Union Pacific R. Co.*, 86 F. (2d) 637 (C. C. A. 2nd, 1936); *A. G. Hull v. Commissioner*, 87 F. (2d) 260 (C. C. A. 4th, 1937); *McNaghten v. United States*, 17 F. Supp. 509 (Ct. Cls., 1937).

In *Commissioner v. Union Pacific R. Co.*, supra, the taxpayer had sold property at a profit in 1917 and 1920, but had erroneously reported such sales as being taxable in 1926. After the statute of limitations had run on 1917 and 1920, the taxpayer sought to have its tax liability for 1926 determined upon a correct basis by eliminating from its 1926 income the profit which should properly have been reported in 1917 and 1920. The Circuit Court of Appeals for the Second Circuit rejected the Commissioner's plea

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[12] In the 1929 return the 50 shares were shown to have been acquired in 1918 at a cost of $500.00 and to have been sold in 1929 for $26,250.00, resulting in a profit of $25,750.00 (R. 29). A Revenue Agent examining the 1929 return would have known that the correct basis of any stock acquired from the decedent was its value on December 12, 1928, rather than its cost in 1918; and could scarcely have failed to conclude that the mistake was one against the taxpayer's interest, since it was highly improbable that the 50 shares increased in value from $500.00 to $26,250.00 during the interval between December 12, 1928, and the date of sale in 1929.

of estoppel, holding that the person claiming the benefit of estoppel must have been ignorant of the true facts and must have been adversely affected by the acts of the person against whom the estoppel is claimed; that the Commissioner had timely knowledge of all the material facts; and that there was therefore no estoppel. The Commissioner did not apply for certiorari.

In *A. G. Hull v. Commissioner,* supra, the taxpayer received a large sum as consideration for granting an option. The Commissioner sought to tax such sum as income for 1926. The taxpayer claimed that such sum was income in 1925, if at all. The Commissioner claimed estoppel on the ground that such income had not been reported by the taxpayer in 1925, and the statute of limitations had run on the collection of additional tax for 1925. The Circuit Court of Appeals for the Fourth Circuit held that there was no estoppel since the Commissioner had full knowledge of all the material facts before the statute ran. The Commissioner did not apply for certiorari.

In *McNaghten v. United States,* supra, the taxpayers sued to recover certain taxes overpaid by them for 1927. The Government sought to defend on the ground that a certain trust, of which these taxpayers were beneficiaries, had failed to pay its proper tax for 1927, the statute of limitations having run against collection of such tax from the trust. The Court of Claims rejected this defense, holding inter alia, that there was no basis for estoppel, since all the facts necessary to a determination and assessment of the taxes against the trust were fully known to the Commissioner 8½ months before the statute ran. The Government did not apply for certiorari.

In the case at bar, the Commissioner was not ignorant of the true facts and was not adversely affected by the acts

of the petitioner, but on the contrary, had timely knowledge of all the material facts as disclosed in the estate tax return, and was in no way misled by the petitioner. There is therefore no estoppel in this case.

III.

THE ISSUE OF RECOUPMENT IS NOT OPEN UNDER THE PLEADINGS IN THIS CASE.

The respondent, in opposing the granting of certiorari in this case, urged that the decision of the Circuit Court of Appeals was rested on the ground of recoupment, although the decision of the Circuit Court of Appeals does not mention the term "recoupment", and does not indicate that the Court relied in any way upon the doctrine of recoupment or any principle analogous thereto.

In its pleadings and at the trial of the case in the District Court the respondent relied solely upon the defense of estoppel. No claim of recoupment was made in the pleadings; no claim is made therein that the alleged tax for 1928 should be set off against or used to reduce or wipe out petitioner's claim for the refund of the overpayments for 1929, 1930 or 1931. The amount of the alleged underpayment of tax for 1928 is nowhere stated in the respondent's pleadings, nor is any indication therein given as to whether such amount is greater or less than the amount which petitioner sued for.

A plea of recoupment must be as definite and certain as though it were an original cause of action. See *Campbell v. Trunnell,* 67 Ga. 518; *Whitt v. Blount,* 124 Ga. 671; *Atlanta Glass Company v. Noizet,* 88 Ga. 43; *McGuire v. Gerstley,* 204 U. S. 489. Clearly the respondent's pleadings in this case fail to meet the foregoing requirements. *Of*

particular significance is the fact that nowhere do such pleadings set forth any amount sought to be recouped. The pleadings were in no way calculated to put the trial judge on notice that the respondent intended to rely upon any such defense.

The only evidence offered by petitioner or respondent at the trial of the case, which could conceivably support a defense of recoupment, is contained in the stipulation designated as defendant's Exhibit A (R. 46-49). That stipulation was offered solely in support of respondent's plea of estoppel and was rejected by the trial court on the ground that the defense of estoppel would not be established, even though the stipulation were admitted (R. 55).

The stipulation just referred to was properly excluded for the reason that it was irrelevant, in that it failed to support the defense of estoppel in connection with which it was offered. Furthermore, even if such stipulation had been offered to prove recoupment, as was not the case, such stipulation should not have been received to prove recoupment, since recoupment was not pleaded and since the evidence must conform to the pleadings. See *Garrett v. L. & N. Railroad Company,* 235 U. S. 308; *Pirkle v. Cooper,* 113 Ga. 828; *Groover v. Simmons,* 163 Ga. 778; *Louisville & Nashville R. Co. v. Barrett,* 143 Ga. 742.

The trial court therefore properly excluded the respondent's Exhibit A and there is therefore no evidence at all in the record to support any belated claim of recoupment by the respondent. Certainly the respondent cannot come in at this late date and assert a defense of recoupment on a record where no recoupment was pleaded or raised in any way in the trial court.

In any event, as is shown under Heading IV below, there is no basis for the respondent's defense based on

the alleged tax for 1928, whether that defense be called estoppel or recoupment or however it may be designated.

IV.

THERE ARE NO SPECIAL EQUITIES IN THIS CASE WHICH WILL PERMIT THE RESPONDENT TO DEFEND ON THE GROUND OF THE ALLEGED TAX FOR 1928.

It is clear that when a taxpayer sues for refund of income taxes which have been overpaid, the Government does not establish a defense by merely showing the existence of a barred tax claim against the taxpayer for some prior year, unless there are circumstances establishing some such connection between the barred tax and the refund sought, as to render the refund claim inequitable.

The most common type of case in which such equitable circumstances exist, and in which the Government may therefore defend on the ground of the barred tax, is the case where the taxpayer has taken some position resulting in non-payment of the earlier year's tax, and thereafter, when the statute of limitations has run on the collection of such earlier year's tax, has sought, by refund suit or otherwise, to take another position inconsistent with the prior position which resulted in non-payment of the earlier year's tax. In such cases where the taxpayer seeks, at the Government's expense, to take an inconsistent position with regard to the same matter, the courts have been liberal in permitting the Government to assert the barred tax claim as a defense, on the theory of estoppel, recoupment or otherwise.

No such situation exists in the case at bar. In the case

at bar, the petitioner is not seeking to change any position which resulted in loss of revenue to the Government. The only error which petitioner is seeking to correct in this case is the error innocently made by the petitioner in overpaying its taxes for 1929, 1930 and 1931, and that error had absolutely no connection whatever with the Government's failure to collect the alleged tax for 1928. The petitioner's claim that it is entitled to recover the taxes which it overpaid for 1929, 1930 and 1931 is in no way inconsistent with any position which petitioner has ever taken with respect to the alleged tax for 1928. This is not a case of there being a certain amount of income which must necessarily fall in one year or the other. The petitioner's case does not rest in any way on showing that the taxes were due in 1928 instead of in 1929, 1930 and 1931.

The alleged tax for 1928 became due, if at all, solely by reason of the decedent's death while owning the installment obligations in question, and nothing which has been done or which can now be done by the petitioner with reference to its taxes for 1929, 1930 or 1931 can possibly have any bearing whatsoever upon the question of whether or not such tax became due for 1928 under Section 44(d).

The petitioner's taxes were overpaid for 1929, 1930 and 1931 because in computing the taxable income for those years from the collection of the installment obligations in question, the petitioner erroneously used, as the basis for determining such income, the original cost of the stock to the decedent, whereas petitioner should have used, as such basis, the value of the installment obligations at the date of decedent's death—an error which has absolutely no connection whatsoever with the entirely independent question of whether any tax became due for 1928 under Section 44(d).

The situation in this case is therefore entirely different from that involved in *Stone v. White*, 301 U. S. 532, 57 S. Ct. 851, and similar cases. In *Stone v. White*, the income there in question was admittedly taxable either to the trustee or to the beneficiary. The trustee could not claim exemption from the tax on such income without conceding at the same time that such income was taxable to the beneficiary, and vice versa. In the case at bar, there is no such "either-or" relation between the overpayments for 1929, 1930 and 1931, on the one hand, and the alleged tax for 1928, on the other. Denial of the tax liability for 1929, 1930 and 1931 is in no way a concession that the alleged tax for 1928 was due. As a matter of fact, the petitioner has contended vigorously throughout each stage of this case that no tax is due for 1928 for the reasons set out under Heading I of this brief.

It follows that the Government may not assert the alleged tax for 1928 as a defense on any theory that the petitioner is seeking to take any inconsistent position at the Government's expense.

The Government is also frequently permitted to assert a barred tax claim as a defense to a refund suit in cases where the taxpayer has in some way caused the Government's failure to collect the barred tax. Under Heading II of this brief, it has been shown that the Government's failure to collect the alleged tax for 1928 under Section 44(d) was in no way caused by the petitioner, but that, on the contrary, the petitioner disclosed all of the material facts in the estate tax return long before the statute of limitations ran, and at no time made any misrepresentations to the Government with respect to the facts giving rise to such alleged tax for 1928 under Section 44(d). The respondent did not offer any evidence whatsoever to show

that the Commissioner's failure to collect the alleged tax for 1928 was in any way caused by any act of the petitioner. There is therefore no basis for allowing the respondent to assert the alleged tax for 1928 as a defense on any theory that the Government's failure to collect that tax was in any way caused by the petitioner.

In determining whether or not the Government may defend on the ground of a barred tax, consideration may be given, in a proper case, to the fact that the Government's failure to make a timely collection of the barred tax was excusable by reason of adverse court decisions, later reversed. In *Stone v. White,* supra, this Court took cognizance of the Government's inability to protect itself under such circumstance, and undoubtedly such circumstance was a moving factor in that decision. In the case at bar no excuse can be found for the Government's failure to make a timely collection of the alleged tax for 1928 under Section 44(d). The material facts giving rise to such alleged tax were all timely disclosed by the petitioner in the estate tax return, and the Commissioner was bound by no interpretation of the law, except his own, with respect to the question of applying Section 44(d). See *McNaghten v. United States,* 17 F. Supp. 509, at p. 515 (Ct. Cls., 1937), recognizing the distinction just pointed out.

In *Stone v. White,* supra, there is some intimation that the Government might be permitted to assert a barred tax claim to defeat a refund claim for a later year, if it appeared that the overpayment for the later year was made before the statute of limitations barred the collection of tax for the earlier year. In the case at bar all but $230.07 of the amount here sued for was paid *after* the statute of limitations expired on the collection of additional tax for

1928.[13] There is therefore no basis for suggesting that the overpayments here sought to be recovered (other than the $230.07 referred to above) should be applied to discharge the alleged tax for 1928, which alleged tax was already barred by the statute of limitations at the time when such overpayments (other than the $230.07 referred to above) were made.

It appears then that the petitioner is not seeking in this suit to take any inconsistent position at the Government's expense; that the petitioner is not seeking to change any position previously taken by it with reference to the alleged tax for 1928; that the Commissioner's failure to collect the alleged tax for 1928 was in no way caused by any action of the petitioner; that the material facts were all disclosed to the Commissioner in the estate tax return long before the statute of limitations ran on 1928; that the Commissioner's failure to collect the alleged tax for 1928 is not excusable in any way, since the Commissioner had timely knowledge of all the facts, and was bound by no interpretation of the law except his own; that with the exception of $230.07 all of the overpayments sought to be recovered in this suit were paid after the statute of limitations had already barred collection of the alleged tax for 1928; and that there are therefore no special equities of any sort to support the respondent's assertion of the alleged tax for 1928 as a defense. In the absence of such special equities, the respondent's defense is no more than

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[13] The decedent's 1928 income return was filed March 12, 1929 (R. 46) and the two year statute of limitations under Section 275 of the 1928 Revenue Act therefore expired on March 12, 1931. The entire overpayments for 1930 and 1931 were paid after March 12, 1931 (R. 6, 18, 10, 21); and the overpayment for 1929 alone was paid prior to March 12, 1931. The overpayment for 1929 sought to be recovered in this suit is only $230.07 (R. 2-5).

an effort to offset such alleged tax for 1928 against petitioner's right to recover the overpayments sued for. In *Stone v. White,* supra, this Court clearly indicated that the Government may not thus assert a barred tax claim by way of offset, in the absence of special equities which, as shown above, are not present in this case.

CONCLUSION.

For the reasons set forth above, it is respectfully submitted that the judgment of the Circuit Court of Appeals should be reversed, and the judgment of the District Court should be affirmed.

Respectfully submitted,

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APPENDIX A.

Revenue Act of 1926, c. 27, 44 Stat. 9.

Sec. 212(d). Under regulations prescribed by the Commissioner with the approval of the Secretary, a person who regularly sells or otherwise disposes of personal property on the installment plan may return as income therefrom in any taxable year that proportion of the installment payments actually received in that year which the total profit realized or to be realized when the payment is completed, bears to the total contract price. In the case (1) of a casual sale or other casual disposition of personal property for a price exceeding $1,000, or (2) of a sale or other disposition of real property, if in either case the initial payments do not exceed one-fourth of the purchase price, the income may, under regulations prescribed by the Commissioner with the approval of the Secretary, be returned on the basis and in the manner above prescribed in this subdivision. As used in this subdivision the term "initial payments" means the payments received in cash or property other than evidences of indebtedness of the purchaser during the taxable period in which the sale or other disposition is made.

* * * * * * *

Sec. 1208. The provisions of subdivision (d) of section 212 shall be retroactively applied in computing income under the provisions of the Revenue Act of 1916, the Revenue Act of 1917, the Revenue Act of 1918, the Revenue Act of 1921, or the Revenue Act of 1924, or any of such Acts as amended. Any tax that has been paid under such Acts prior to the enactment of this Act, if in excess of the tax imposed by such Acts as retroactively

modified by this section, shall, subject to the statutory period of limitations properly applicable thereto, be credited or refunded to the taxpayer as provided in section 284.

* * * * * * *

Revenue Act of 1928, c. 852, 45 Stat. 791.

Sec. 44. *Installment Basis.*

* * * * * * *

(b) Sales of realty and casual sales of personalty.—In the case (1) of a casual sale or other casual disposition of personal property (other than property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year), for a price exceeding $1,000, or (2) of a sale or other disposition of real property, if in either case the initial payments do not exceed 40 per centum of the selling price, the income may, under regulations prescribed by the Commissioner with the approval of the Secretary, be returned on the basis and in the manner above prescribed in this section. As used in this section the term "initial payments" means the payments received in cash or property other than evidences of indebtedness of the purchaser during the taxable period in which the sale or other disposition is made.

* * * * * * *

(d) Gain or loss upon disposition of installment obligations.—If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and (1) in the case of satisfaction at other than the

face value or a sale or exchange—the amount realized, or (2) in case of a distribution, transmission, or disposition otherwise than by sale or exchange—the fair market value of the obligation at the time of such distribution, transmission, or disposition. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full.

* * * * * * *

Sec. 113. *Basis for Determining Gain or Loss.*

(a) Property acquired after February 28, 1913.—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; except that—

* * * * * * *

(5) Property transmitted at death.—If personal property was acquired by specific bequest, or if real property was acquired by general or specific devise or by intestacy, the basis shall be the fair market value of the property at the time of the death of the decedent. If the property was acquired by the decedent's estate from the decedent, the basis in the hands of the estate shall be the fair market value of the property at the time of the death of the decedent. * * *

APPENDIX B.

ILLUSTRATIVE CASE.

Comparison of Taxable Profit Under Installment Basis With Profit That Could Be Taxed on Some Other Theory.

Facts:

"A" sells property in 1923 for an agreed price of $100,000.00, of which $10,000.00 is paid in cash in 1923 and the balance is represented by nine notes of $10,000.00 each, payable one in each year thereafter for nine years. The property had cost "A" $15,000.00. The purchase money notes of a face value of $90,000.00 had a fair market value of only $9,000.00 at the date of sale. "A" dies in 1927, after having collected $50,000.00 of the agreed price.

Computation of Gain Without Use of Installment Method:

Gain Realized in Year of Sale:		
Cash received in 1923	$ 10,000.00	
Fair market value of notes (10% of $90,000.00 face)	9,000.00	
Total Consideration Realized in 1923	$ 19,000.00	
Cost	15,000.00	
Gain Realized in 1923		$ 4,000.00
Gain on Collection of Notes 1924-1927:		
Amount collected on notes	$ 40,000.00	
Basis (Valuation in determining gain in 1923—10% of face)	4,000.00	
Gain on collection of notes		36,000.00
Total gain		$40,000.00

Computation of Gain on Installment Method:

Agreed Price	$100,000.00	
Cost	15,000.00	
Gross Profit to Be Realized	$ 85,000.00	
Percentage of collections representing profit	85%	
Amount collected during life of "A"	$ 50,000.00	
Profit reported on installment basis		$42,500.00

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1937

No. 6

D. W. McEACHERN, ADMINISTRATOR OF THE ESTATE OF S. C. McEACHERN, DECEASED,

Petitioner,

v.

J. T. ROSE, FORMER COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

REPLY BRIEF FOR PETITIONER.

W. A. SUTHERLAND,
JOSEPH B. BRENNAN,
Counsel for Petitioner.

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In view of certain admissions made in brief for respondent and the consequent narrowing of the issues involved, petitioner is taking the liberty of filing this reply brief. The discussion will follow the order of the respondent's brief.

Respondent's So-Called Equitable Defense.

In respondent's brief the Solicitor General abandons the defense of estoppel (Br. pp. 9-11 n.) and admits that there

is no defense of "strict recoupment" (Br. p. 17). He asserts that the defense is "in the nature of an equitable recoupment,"[1] and that under a general plea of *non assumpsit* he can show any facts which would deny the equity of petitioner's claim (Br. p. 17). This statement overlooks the fact that the Georgia practice, which must be followed under the Conformity Act,[2] does not recognize the plea of *non assumpsit;* and in an action of this kind the only defenses available without affirmative pleading are the non-receipt of the money sued for or its repayment. Georgia Code 1933, Secs. 81-306, 81-307; *Massee* v. *Stetson,* 27 Ga. App. 89; *Walker* v. *Kingston Supply Co.,* 18 Ga. App. 447. It is submitted that respondent's plea was one of estoppel pure and simple[3] and the evidence he tendered was inadmissible under the pleadings. If the evidence offered by respondent was properly excluded, of course petitioner was entitled to judgment.

In attempting to show the "inequity" of allowing petitioner to recover here, respondent claims that the income on which taxes were erroneously paid for 1929, 1930 and 1931, was the same income on which a tax should have been,

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[1] That is, "not the standard article to be marked by the standard label." See *Daube* v. *United States,* 289 U. S. 367, 371.

[2] 28 U. S. C. A. § 724.

[3] It is true that respondent's plea alleged that "it would be unconscionable for the plaintiff to be allowed any recovery from defendant." (R. 17, 20, 23.) However, the statement is based upon alleged circumstances which relate only to estoppel. The plea cannot have the faintest flavor of recoupment where it does not indicate the amount of the 1928 tax which the Government has lost. On the other hand, if the remaining elements of estoppel were present a lost tax of $10 for 1928 would be sufficient detriment to the Government to warrant the application of estoppel. Moreover, respondent's affirmative plea concludes with a claim of estoppel based upon what has gone before.

In the cases of *Stone* v. *White,* 301 U. S. 532, and *Bull* v. *United States,* 295 U. S. 247, the amounts of the taxes underpaid and overpaid, respectively, were distinctly set up in the pleadings.

but was not, paid for 1928. Even if the same income were involved[4] it will be apparent that there would be no equitable basis for denying recovery in this case.

Respondent's argument at its best amounts to this: Petitioner erroneously paid a tax on certain income as income for 1929, 1930 and 1931; petitioner should have paid a greater tax for 1928 on the same income; therefore the payments made were erroneous only because they were identified as taxes for the wrong year. The simple answer to that argument is that the amounts paid for 1930 and 1931[5] would be refundable even if they had been paid and received as taxes for 1928. This follows from the fact that at the time petitioner filed returns for 1930 and 1931, and at the time the taxes for those years were assessed and collected, the statute of limitations had run against assessment and collection for 1928.[6] Under Section 607 of the Revenue Act of 1928 (45 Stat. 791) any amounts collected as tax after the expiration of the limitation period are deemed overpayments and are refundable. Respondent, therefore, cannot properly say that the payments were erroneous *only* because they bore the wrong labels. Even if they had been labelled as 1928 taxes, they were erroneously paid and would constitute refundable overpayments.

Stated another way, respondent's argument is that it is inequitable for petitioner to recover a tax erroneously paid on certain income if the same income has escaped tax on a

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[4] While it should be immaterial for the decision of this case, the collections on the installment obligations received by petitioner in 1929, 1930 and 1931 are not the *same* income which respondent alleges was subject to tax in 1928 on the transmission at death of the said installment obligations. The transmission by death did give rise to taxable income to decedent in 1928 if Section 44(d) is applicable and constitutional; but there was no income on the collection of these obligations by petitioner except a very small amount the tax on which is not now in dispute.

[5] The only amount of 1929 taxes involved is the sum of $230.07.

[6] See petitioner's original brief, p. 30 n.

correct basis. The argument is unsound since it would serve to defeat any action to recover a tax collected after the statute of limitations had run. It is well established that such an action can be maintained although it may result in the taxpayer's recovery of a tax erroneously paid on income which has escaped tax on a correct basis. Even before Section 607 of the 1928 Act, this court allowed recovery in such a case. *Bowers* v. *New York & Albany Lighterage Co.*, 273 U. S. 346.[7] It is submitted that respondent has failed to point out any circumstance in the present case which would render it inequitable for petitioner to recover.

If the Government had been misled into not collecting the tax due for 1928 by anything contained in the returns filed for 1929, 1930, and 1931, and had proved such facts, a different situation might exist. Under such circumstances something in the nature of an estoppel might exist which would prevent a change of the positions taken in these returns. But there is not anywhere in the record the slightest evidence that anything in these returns had any effect whatever in influencing the Commissioner not to collect the taxes alleged to be due for 1928.

If in 1928 the petitioner had taken a position which if correct would require him to take the position he took in his returns for 1929, 1930, and 1931, it might be unfair to permit the petitioner to avoid the results of the position taken in 1928 by taking a position inconsistent with that required by his 1928 return after the statute of limitations has run against collection for that year. But we have no

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[7] The court below relied upon *Moses* v. *Macferlan*, 2 Burr. 1005, in which the court said that an action in assumpsit for money had and received could not be maintained to recover money paid after the statute of limitations had barred payment. Such a principle can have no application in a taxpayer's suit for refund, as this Court has made clear. In a case of that kind the parties are reversed, and the taxpayer is in substance and effect the defendant. See *Bull* v. *United States*, 295 U. S. 247, 260.

such situation here. The taxability or nontaxability of the unpaid installment obligations in the return of the decedent for the year of his death has no relation whatever to the income tax of decedent's estate. The decedent's estate is taxable only on the difference between the value at date of death of property or obligations received from decedent and the amount realized on their disposition or collection. This was the same before Section 44(d) was enacted and after and is the same whether Section 44(d) is constitutional and applicable or not.

The respondent apparently is seeking to establish the existence of some such special equities when on page 14 of his brief he says:

> "The showing by which Petitioner establishes that the income reported was not taxable in those years (1929, 1930 and 1931) discloses that the income was taxable in another year for which it was not reported."

This clearly is not so. In order to show that an excessive amount has been reported as income on the collection, by the estate, of choses in action acquired from the decedent, petitioner needs to show only that the reported amount exceeds the difference between the amount collected and the value of the choses at petitioner's death.

It is immaterial for the purpose of this showing how these obligations were treated in connection with decedent's income tax returns for 1924 or 1928. Whether the income taxes of decedent for either of those years were underpaid or overpaid has nothing to do with the determination of the income of the estate on the collection of these obligations. The only fact of importance is that the obligations became capital in the hands of the estate at their fair market value at the date of the death of the decedent and the Government collected an estate tax upon this basis. This and this alone is made the basis under the law for future determinations of income, and no error for or against the

decedent in the taxation of income to him can in any way affect the income tax computations of the estate.

The respondent relies upon three decisions of this Court as sustaining his position in this case, viz., *Stone* v. *White*, 301 U. S. 532; *Bull* v. *United States*, 295 U. S. 247; and *Lewis* v. *Reynolds*, 284 U. S. 281.

The case of *Lewis* v. *Reynolds* has no bearing upon the present case. It involved taxes for only a single year and the *taxes for that year* admittedly *had not been overpaid.* This Court in denying recovery had only to say, as it did:

> "An overpayment must appear before refund is authorized." 284 U. S., at 283.

The case of *Bull* v. *United States*, far from supporting the position of respondent, seems to support the position of petitioner. The *Bull* case held that an income tax against an estate and an estate tax could not be collected on the same item. Here an estate tax was paid on $80,714.25 out of the $90,000 collected by the estate in 1929, 1930 and 1931, and now the Government claims the right to retain income taxes erroneously paid on all except $1,500 of the $90,000 collected, even though on $80,714.25 of this sum a capital tax (the estate tax) has already been paid. This is exactly what the *Bull* case held could not be done.

The case of *Stone* v. *White, supra,* was discussed in petitioner's original brief. As was there pointed out, it is clearly distinguishable from the present case in several particulars. There a single error resulted in the overpayment by one taxpayer and underpayment by the other. A holding that one party was liable meant that the other was not, and *vice versa.* Here regardless of whether or not a tax was due in 1928 by decedent, clearly no tax was due for 1929, 1930 and 1931. The Commissioner in *Stone* v. *White* was excusable for his error. He was misled by court deci-

sions and could have protected himself legally only by the hardship of assessing both trustee and beneficiary. Here the Commissioner could not have been in any quandary because it was clear to anyone considering the matter that no tax was due for 1929, 1930 or 1931. While, under the modified opinion of this Court in that case, it appears that the taxes were not collected from the trustee before the statute ran against the beneficiary, the Commissioner, however, did *assess* the tax against the trustee before the statute ran against the beneficiary. Here the taxes collected for 1930 and 1931 were assessed and collected after the statute of limitations had run on 1928.[8] In fact, the statute had run even before the returns for these two years were filed. In *Stone* v. *White* the Court does not cut across taxable years and ignore the computations of income on a yearly basis which is an essential part of our present system of income taxation. A decision in respondent's favor here to a large extent must ignore the separation between different taxable years.

Here the respondent's defense amounts to no more than a showing that a tax upon certain income was not collected when it was due. The reason given for the failure to collect the tax is that the income tax return for the year did not show the receipt of this income. This reason, which lies behind the failure to collect a large part of the taxes upon which the statute of limitations runs, does not justify the respondent in failing to follow the express commands of Sections 607 and 609 of the Revenue Act of 1928 by retaining erroneous payments made in later years. The "abstract justice" upon which respondent attempts to justify his illegal retention of these payments would apply in any case where a tax is paid after the statute of limitations has run.

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[8] The foregoing distinction between this case and *Stone* v. *White* is the only distinction that does not apply as well to petitioner's claim for the 1929 overpayment as to overpayments for 1930 and 1931.

If respondent's position were sound, the Government in order to collect any barred tax for any year would have only to assert the liability in any open year on the basis of the inclusion in that year of the income on which tax had not been paid, and then, after the tax had been collected, the Government could defend against its repayment on the ground that it was paid on the same income in connection with which the taxpayer had failed to pay the proper tax in another year. Obviously this Court should not be asked so to hold.

The Unconstitutionality of Section 44(d)

Respondent attempts to support Section 44(d) against constitutional attack by urging that the section should be construed as taxing something other than what it says should be taxed. Section 44(d) provides in so many words that—

> "If an installment obligation is * * * transmitted * * * gain or loss shall result to the extent of the difference between the basis of the obligation and * * * the fair market value of the obligation at the time of such transmission."

Respondent claims, of course, that the section becomes operative when an installment obligation is transmitted by death, but he contends that:

> "This section does not and was not intended to tax any purported income arising from the transmission of the obligation at death." (Resp. Br., p. 22.)

In an effort to save the validity of Section 44(d), the respondent urges that it should be construed as taxing "the remaining unreported profit on the (installment) sale in the year in which the vendor disposes of the (installment) obligations by transmission by death or otherwise." (Resp.

Br., p. 21). It is submitted that the statute cannot be given any such construction.

This Court has made it plain that it will not by usurpation of the legislative function rewrite a statute and give it a meaning it certainly does not have in order to save it from unconstitutionality. In *Heiner* v. *Donnan*, 285 U. S. 312, this Court held invalid the provision of Section 302(c) of the Revenue Act of 1926, creating a conelusive presumption that a gift within two years of the donor's death was made in contemplation of death and was, therefore, subject to the estate tax. The Government attempted to support the provision as being in effect a tax on certain gifts *inter vivos*. In repudiating that contention, this Court said:

> "It is so apparent from a consideration of these features of the statute that Congress could not have had, even remotely, in mind the imposition of a gift tax, that to construe the provision in question as imposing such a tax is to disregard the plain language and the plain intent of the act. For this court to do so would be to enact a law under the pretense of construing one and thus pronounce itself guilty of a flagrant perversion of the judicial power." 285 U. S. at 331.

It is impossible to construe Section 44(d) as imposing a tax in the year of the seller's death on the unreported profit resulting from the installment sale. This was demonstrated in our original brief where we pointed out, *inter alia*, that the fair market value of the installment obligations outstanding at death, which is an essential element in a computation of gain under Section 44(d), can have nothing to do with the profit realized on the sale and on the collection of prior installments.

Respondent's brief admits that the "profit" taxable under Section 44(b) and (d) would be greater than the profit which could have been taxed to the seller under at

least two methods of computation. (Resp. Br., pp. 30, 31). But respondent urges that there is a third method of computation which if applied here would show the same taxable profit to the seller as is shown under Section 44(b) and (d). (Resp. Br., pp. 31, 32). The "third method" might be questioned as a proper measure of "income", within the meaning of the Sixteenth Amendment. The view that the earlier deferred payments contain a larger percentage of profit than the later ones does not fit in with the popular conception of income which limits the congressional power.[9]

But in any event, Section 44(d) does not undertake to apply this "third method". It may be that in some cases the results will be the same. It would seem that the amount taxable under the "third method" would equal the amount taxable under Section 44(b) and Section 44(d) together, only (1) if the assumed rate of discount remained constant from year to year and (2) if the payments received up to the seller's death are not too small to reflect the accumulated discount on the remaining payments.

In the computation set out in Appendix B of respondent's brief, the results under the "third method" and Section 44(b) and (d) are shown to be the same *only because a constant rate of discount is arbitrarily assumed and a figure is taken as representing the 1924 market value of the purchase money obligations which does not have anything to support it.* It cannot be assumed that the extent of discount reflected by the fair market value of the obligations outstanding at the seller's death in 1928 can be used to determine the fair market value of all deferred payments at the time of sale in 1924. There is more than the element of time in determining the value of such obligations. If the risk element is to be ignored, as respondent has ignored it, there

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[9] *Eisner* v. *Macomber*, 252 U. S. 189, 206; *United States* v. *Safety Car Heating and L. Co.*, 297 U. S. 88, 99.

would be no reason why the rate of discount here would differ from that on Treasury notes.

The risk element is variable in these cases. Security may become more or less valuable as maturity approaches. Here the stock which was sold was originally pledged to secure 90 per cent of the selling price,—leaving a small margin of security. At the seller's death, the same amount of stock secured only 50 per cent of the original selling price.

If the "third method" advanced by respondent can ever have a place in determining taxable income under the Sixteenth Amendment, it must be clear that such a method is not incorporated in Section 44(d). If the results are the same in any case under Section 44(b) and (d) as under that method, it is because by mere chance the discount reflecting the value of installment obligations at death is based on the same rate as the discount reflecting value at the date of sale.

Respondent suggests that petitioner's constitutional objections can be disposed of on the ground that the evidence does not show that the tax under Section 44(d) (stipulated to be $11,625) is any greater than the tax which might have been collected for 1924 (the year of sale) on the excess of cash and fair market value of deferred payments over the cost of the property sold. (Resp. Br., pp. 26, 27). There was, of course, no evidence as to the market value (if any) of the installment obligations in 1924; and it, therefore, does not appear what amount could have been taxed as gain in that year if the installment method had not been used. But that circumstance is of no importance. A tax on a fictitious "gain" in 1928 cannot be sustained on the ground that the taxpayer has failed to show that a tax could not have been imposed upon him in as great an amount in 1924. Respondent's argument could be just as logically applied to deny a refund of a tax collected on a stock dividend, on the ground that the taxpayer had the benefit of certain de-

ductions which Congress did not have to, but did, allow, and which, if disallowed, would result in the taxpayer's having paid a correct amount of tax.

As we have demonstrated, Section 44(d) does *not* undertake to tax the unreported portion of a profit that could have been taxed in earlier years, and the nature and extent of such profit is immaterial here.[10]

Respectfully submitted,

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Counsel for Petitioner.

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[10] If evidence of the value of the obligations at the time of sale had been material to a consideration of the constitutional question, petitioner has not yet had an opportunity to adduce such evidence. Petitioner did raise his constitutional objection when respondent offered evidence in support of his affirmative defense (R. 49). The trial judge, however, excluded respondent's evidence on non-constitutional grounds (R. 49). If respondent's evidence had been admitted, petitioner would have been expected only then to offer any evidence that might be necessary to overcome the defense.

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132628—37——1

In the Supreme Court of the United States

OCTOBER TERM, 1936

No. 750

D. W. MCEACHERN, ADMINISTRATOR OF THE ESTATE OF S. C. MCEACHERN, DECEASED, PETITIONER

v.

J. T. ROSE, FORMER COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

There was no formal opinion by the District Court. The opinion of the Circuit Court of Appeals (R. 76–81) is reported at 86 F. (2d) 231.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on November 9, 1936 (R. 81). By order of the Honorable Benjamin N. Cardozo, As-

sociate Justice of this Court, on February 1, 1937, the time for filing a petition for a writ of certiorari was extended to and including February 24, 1937 (R. 86). The petition for writ of certiorari was filed February 23, 1937. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the petitioner is entitled to recover the amounts of income taxes overpaid for the years 1929, 1930, and 1931, where a larger amount of income tax due from the petitioner for the year 1928 on income arising from the same transaction remained unpaid, collection of the 1928 tax being barred by the statute of limitations.

STATUTE INVOLVED

The Revenue Act of 1928, c. 852, 45 Stat. 791, provides in part as follows:

SEC. 44. INSTALLMENT BASIS.

* * * * *

(d) *Gain or loss upon disposition of installment obligations.*—If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and (1) in the case of satisfaction at other than face value or a sale or exchange—the amount realized, or (2) in case of a distribution, transmis-

sion, or disposition otherwise than by sale or exchange—the fair market value of the obligation at the time of such distribution, transmission, or disposition. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full.

STATEMENT

The facts, developed by stipulations (R. 51–58, 60–62), may be summarized as follows:

Petitioner (hereinafter referred to as the estate) is the administrator of the estate of S. C. McEachern, deceased (R. 76–77).

On September 3, 1924, S. C. McEachern, the decedent, sold 500 shares of the capital stock of the Industrial Life & Health Insurance Company for the sum of $300,000. The contract of sale provided that $30,000 was to be paid in cash and the balance in quarterly installments of $7,500 each, payable on March 1, 1925, and on the first day of every third month thereafter. The stock had cost the decedent $10 a share, or a total of $5,000. (R. 77.) In reporting his profit from the sale, the decedent in his lifetime elected to and did report his gain on the installment basis for the years 1924, 1925, 1926, and 1927 (R. 20, 23, 27).

On December 12, 1928, with installments aggregating $150,000 still unpaid, he died intestate (R. 77). On the date of death the unpaid installments had a fair market value of $125,000, arrived

at by discounting their face value ($150,000) at 6.348% per annum from the date of death to the due dates of the installments (R. 52). In the estate tax return there was listed among the assets of the estate "Unpaid balance of deferred payments on 250 shares of stock of Industrial Life & Health Insurance Company under contract between S. C. McEachern and J. N. McEachern, as Trustee, dated September 3, 1924—$125,000.00" (R. 51).

The estate filed income tax returns for 1929, 1930, and 1931, reporting in each year as income the profits on the installments collected in each year, based on the cost of the stock to the decedent, the item in each return being shown as a complete sale of 50 shares made during the year and not as collections on the installment obligations (R. 36, 41, 46, 77–78). By this suit the estate sought the recovery of alleged overpayments (aggregating $3,858.34) of income taxes in those three years, asserting that the income reported was excessive for the reason that only the excess of the respective installments collected over the fair market value of the unpaid installment obligations at the date of decedent's death constituted income to the estate (R. 1–18).

The Government defended on the ground that the estate was not entitled to recover the claimed overpayments of income taxes ($3,858.34) for the years 1929, 1930, and 1931, because a larger amount ($11,625) of income tax for the year 1928, on income arising from the same installment obliga-

tions, was due from the estate and remained unpaid, its collection being barred by the statute of limitations (R. 19–30). The Government contended that under the provisions of Section 44 (d) of the Revenue Act of 1928, *supra,* p. 2, in the income tax return filed by the estate for the income of decedent from January 1, 1928, to date of death, December 12, 1928, a gain should have been reported at the time of the transmission by death of the unpaid installment obligations, but that the said 1928 income tax return did not include such gain; that if such gain had been included, pursuant to Section 44 (d), then "an additional tax in the sum of $11,625.00 would be due and unpaid" (R. 61) by the estate on account of the income tax liability of the decedent for the period from January 1, 1928, to December 12, 1928. The Government further argued that the estate, by reason of its conduct in making out the income tax returns for the income of the decedent in 1928 and the income of the estate in 1929, 1930, and 1931, in an incorrect and misleading manner as above stated, should not now, limitation having barred the collection of the larger tax due for 1928, be entitled or permitted to recover the alleged overpayments made on the incorrect returns for 1929, 1930, and 1931 (R. 19–30, 60–62, 77–78).

When the claims for refund upon which this suit is founded were filed, the time for making an additional assessment for the 1928 period had already expired (R. 5, 10, 15–16, 60).

The estate took the position that it was not, under the facts, precluded from recovery of the overpayments in question, and, further, that Section 44 (d), upon which the larger tax for 1928 is based, is unconstitutional (R. 62–64, 79). The District Court regarded the facts as not constituting an estoppel or otherwise operating to defeat the suit, and not therefore passing on the constitutionality of Section 44 (d), directed a verdict and entered judgment in favor of the estate (R. 31,-32, 64, 67). The Circuit Court of Appeals reversed the judgment of the District Court and held, first, that Section 44 (d) is constitutional; and, second, that the estate was not entitled to recover the overpayments for 1929, 1930, and 1931 on the income from the installment obligations because a larger amount of income tax due for the year 1928 on the same installment obligations remained unpaid, and hence the estate could not claim that the defendant collector "has money which, ex aequo et bono, the defendant ought to refund" (R. 76–80). The court concluded that the estate could not use a suit for refund to obtain money which the estate "ought not in good conscience, to have back" (R. 81).

ARGUMENT

The petition proceeds on the theory that the decision of the Circuit Court of Appeals is on the ground of estoppel. As reasons for granting the writ it is urged (Pet. 5–6) that the decision below is in conflict with the decisions on the question of

estoppel in the cases of *Salvage* v. *Commissioner,* 76 F. (2d) 112 (C. C. A. 2d), affirmed, 297 U. S. 106; *Commissioner* v. *Union Pacific R. Co.,* 86 F. (2d) 637 (C. C. A. 2d); *Hull* v. *Commissioner* (C. C. A. 4th), decided January 5, 1937, not officially reported but found in 1937 Prentice-Hall, Vol. I, p. 1078; that the question of estoppel in Federal income tax cases is important; and that the decision of the court below in the instant case is similar, on the question of estoppel, to the decision in *Commissioner* v. *Farren,* 82 F. (2d) 141 (C. C. A. 10th), in which this Court granted certiorari (298 U. S. 653), but which was dismissed by stipulation of the parties on October 26, 1936. In the brief in support thereof, the conflicts above mentioned with decisions on estoppel, the importance of the question of estoppel in income tax cases, and the similarity to the decision on estoppel in the *Farren* case are discussed (pp. 9–17).

The decision of the Circuit Court of Appeals does not rest on estoppel. It rests on recoupment. It is submitted, therefore, that the reasons advanced for the granting of the writ are without merit.

The court below, in its opinion, expressly stated (R. 80) that its decision was not based upon estoppel. The court said (R. 79–80):

> We come then, to consider appellee's case as it really stands, the case of one who, though on a correct basis should have paid considerably more as taxes on account of

> these installment obligations than he has paid on an incorrect basis, cannot, because of the course he has taken, limitation having now run, be made to pay on the correct basis. So considering it, we think it perfectly plain that though the sums he paid were paid on a particular theory of obligation which did not exist, he may not recover these sums back because they are in sum less than the amount which on a correct theory of obligation, he ought to have paid on account of these installment obligations. This is so not because of the existence of a technical estoppel or a waiver, but because his action was equitable in its nature and grounds, and he may not succeed in it unless he can show that the defendant has money which, ex aequo et bono, the defendant ought to refund.

In *Lewis* v. *Reynolds,* 284 U. S. 281, this Court has definitely recognized the right of the United States to recoupment of an unpaid tax even where the collection of it would be barred by limitation. In *Bull* v. *United States,* 295 U. S. 247, this Court reaffirmed the applicability of recoupment by way of defense to a demand for taxes. It is established by a long line of authorities that recoupment is particularly applicable to actions for the recovery of taxes, because such an action is in the nature of an action for money had and received, which, although in form at law, is governed by equitable principles, and because in such an action a plaintiff cannot recover unless he can show that in

equity and good conscience he is entitled to money which the defendant *ex aequo et bono* should pay back. *Bull* v. *United States, supra; Lewis* v. *Reynolds, supra; United States* v. *Jefferson Electric Co.,* 291 U. S. 386; *United States Paper Exports Ass'n* v. *Bowers,* 80 F. (2d) 82 (C. C. A. 2d); *Hartwell Mills* v. *Rose,* 61 F. (2d) 441 (C. C. A. 5th); *Champ Spring Co.* v. *United States,* 47 F. (2d) 1 (C. C. A. 8th), certiorari denied, 283 U. S. 852; *New York Life Insurance Co.* v. *Anderson,* 257 Fed. 576 (S. D. N. Y.); *Crossett Lumber Co.* v. *United States* (C. C. A. 8th), decided February 8, 1937, not officially reported but found in 1937 Prentice-Hall, Vol. I, p. 1294; *Lit* v. *United States,* (E. D. Pa.), decided February 26, 1937, not officially reported but found in 1937 Prentice-Hall, Vol. I, p. 1326. As this Court said in the *Jefferson Electric* case, at page 402:

> * * * the statutes providing for refunds and for suits on claims therefor proceed on the same equitable principles that underlie an action in assumpsit for money had and received. Of such an action it rightly has been said:
>
> "This is often called an equitable action and is less restricted and fettered by technical rules and formalities than any other form of action. It aims at the abstract justice of the case, and looks solely to the inquiry, whether the defendant holds money, which *ex aequo et bono* belongs to the plaintiff. It was encouraged and, to a great extent, brought into use by that great

> and just judge, Lord Mansfield, and from his day to the present, has been constantly resorted to in all cases coming within its broad principles. It approaches nearer to a bill in equity than any other common law action."

In such an action to recover taxes the defendant can assert by way of defense a counterdemand for recoupment of a claim arising from the same transaction as that which is the basis of the plaintiff's suit. And it is immaterial that the counterdemand would be barred by the statute of limitations. As this Court stated in *Bull* v. *United States, supra* (p. 262):

> * * * recoupment is in the nature of a defense arising out of some feature of the transaction upon which the plaintiff's action is grounded. Such a defense is never barred by the statute of limitations so long as the main action itself is timely.

Hence in the instant case the Government was entitled to recoupment of its claim for the 1928 tax which arose from the same transaction out of which the estate's claim arose; and the court below correctly so decided. *Bull* v. *United States; Lewis* v. *Reynolds; Crossett Lumber Co.* v. *United States; United States Paper Exports Ass'n.* v. *Bowers; Champ Spring Co.* v. *United States; Lit* v. *United States;* all *supra.*

A word may be said about the attack upon the constitutionality of Section 44 (d), which was

made below. Although such charge is reasserted in the specifications of error (No. 4, Pet. 8), nothing is said in support thereof in the brief. The court below held that the section was constitutional (R. 79). Other courts have uniformly held it constitutional (*Provident Trust Co. of Philadelphia* v. *Commissioner,* 76 F. (2d) 810 (C. C. A. 3d); *Crane* v. *Helvering,* 76 F. (2d) 99 (C. C. A. 2d); *Nuckolls* v. *United States,* 76 F. (2d) 357 (C. C. A. 10th)) even where the installment sale was made, as here, before the passage of the 1928 Revenue Act. *Lawler* v. *Commissioner,* 78 F. (2d) 567 (C. C. A. 9th); *Moore* v. *United States,* 10 F. Supp. 143 (C. Cls.), certiorari denied, 296 U. S. 583.

CONCLUSION

The decision of the Circuit Court of Appeals is correct and is in accord with applicable decisions of this Court and of inferior courts. There is no conflict of decisions. The petition should be denied.

Respectfully submitted.

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MARCH 1937.

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In the Supreme Court of the United States

OCTOBER TERM, 1937

No. 6

D. W. McEACHERN, ADMINISTRATOR OF THE ESTATE OF S. C. McEACHERN, DECEASED, PETITIONER

v.

J. T. ROSE, FORMER COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Circuit Court of Appeals for the Fifth Circuit (R. 57–62) is reported in 86 F. (2d) 231. There was no opinion of the District Court, the case being tried before a jury and both parties moving for a directed verdict.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on November 9, 1936 (R. 62). On February 1, 1937, Mr. Justice Cardozo entered an

order of this Court extending the time for filing a petition for certiorari in the case at bar to and including February 24, 1937 (R. 67). The petition for a writ of certiorari was filed February 23, 1937, and was granted April 5, 1937 (R. 67). The jurisdiction of this Court is conferred by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. In a suit to recover taxes paid on income erroneously reported in returns for 1929, 1930, and 1931 was evidence that the income should have been reported in the return for 1928, and a much larger tax paid thereon, properly admissible as a defense?

2. Is Section 44 (d) of the Revenue Act of 1928 constitutional?

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved will be found in the Appendix, *infra,* pp. 37–47.

STATEMENT

On September 3, 1924, S. C. McEachern, the decedent, sold 500 shares of the capital stock of the Industrial Life & Health Insurance Company to J. N. McEachern for the sum of $300,000, $30,000 of which was to be paid on that day in cash. The balance, under the contract of purchase, was payable in quarterly installments of $7,500 each, the first being due March 1, 1925, and "a like sum of

$7,500.00 on the first day of each and every third month thereafter until the full balance of $270,000.00 is fully paid" (R. 3, 14). The cost basis of this stock in the hands of decedent was $10 per share, which was the price paid by him for said stock (R. 47).

Decedent chose to treat this sale as an installment sale for income tax purposes under the applicable regulations, and during the years prior to his death he reported the proportionate profits on the respective installments collected in each year, based on the original cost of the stock to decedent, as income (R. 16, 19, 22). Decedent died intestate on December 12, 1928. On February 4, 1929, letters testamentary were granted upon the estate of the decedent to D. W. McEachern, the present petitioner, and on the same day the said D. W. McEachern qualified as administrator of the estate (R. 1).

In filing income tax returns for the estate for the years 1929, 1930, and 1931, the administrator reported as income the proportionate profits on the respective installments collected in each of said years, based on the original cost of the stock to decedent, and paid the taxes for said periods upon that basis (R. 40–45). These returns did not indicate that the items referred to represented collections on installment obligations, but, on the contrary, indicated that the items represented separate sales of stock occurring during each taxable year (R. 26–39).

On December 9, 1932, petitioner filed his claims for refund of the taxes paid on those installments for the years 1929, 1930, and 1931, aggregating $3,858.34, urging that the installments were not income except to the extent that they exceeded the fair market value at the death of decedent of the right to receive the remaining installments (R. 4, 8, 13). These claims for refund were rejected by the Commissioner of Internal Revenue on May 17, 1933, and the petitioner was duly advised of said action on that date (R. 4, 8, 13). This suit was thereupon commenced by the petitioner for the recovery of the amounts so paid.

In his answer respondent did not contest the fact that the taxes sued for were erroneously reported and paid in the years 1929, 1930, and 1931. However, respondent set up an affirmative defense to each count, in which it was alleged that the income upon which the taxes sued for were paid should have been reported by petitioner and a tax paid thereon in the return filed on behalf of the decedent for the year of his death, namely, 1928. The affirmative defenses further alleged that in view of this fact it would be unconscionable to allow petitioner a recovery in this case, and that petitioner was estopped from such a recovery (R. 15–24).

At the trial respondent offered in evidence a stipulation showing the following facts: On March 12, 1929, petitioner, as administrator of the estate of S. C. McEachern, deceased, filed with the Col-

lector of Internal Revenue an income tax return on behalf of said S. C. McEachern for the period from January 1, 1928, to December 12, 1928, the date of the death of said S. C. McEachern. The income tax due according to said return was $1,441.70, which was duly paid. The return shows the sale of fifty shares of Industrial Life & Health Insurance Company stock, with a net profit of $29,500. The return did not show that the profit referred to was derived from a collection on an installment obligation. In the return petitioner did not include any gain or profit received by the said S. C. McEachern which was taxable at the time of the transmission by death from the said S. C. McEachern to his estate of the installment obligations remaining unpaid under the contract of September 3, 1924. Under Section 44 (d) of the Revenue Act of 1928 a gain based on the remaining installment obligations should have been reported in the return for the period of January 1, 1928, to December 12, 1928, and an additional tax in the sum of $11,625 paid thereon (R. 46–48).

On the date of filing by petitioner of the claims for refund of the taxes paid for the years 1929, 1930, and 1931, upon which this action is based, the time for making an additional assessment of taxes for the 1928 period had expired (R. 19–30).

The petitioner objected to the introduction of the stipulation offered by respondent, and the objection was sustained on the ground that the facts

covered by this stipulation were irrelevant, in that they undertook to support a defense of estoppel, and even though the stipulation were admitted, estoppel would not be established (R. 49). To this ruling respondent duly excepted (R. 49).

Petitioner offered in evidence certain paragraphs of another stipulation showing that the Federal estate tax return filed for the estate of S. C. McEachern by petitioner listed among the assets of the estate "an unpaid balance of deferred payments on 250 shares of stock of the Industrial Life & Health Insurance Company under contract between S. C. McEachern and J. N. McEachern, as trustee, dated September 3, 1924 * * * $125,000" (R. 39). Respondent objected to the admission of this evidence, but the objection was overruled (R. 45–46).

On the date of the death of S. C. McEachern, the unpaid installment obligations were of a face value of $150,000, and had a fair market value of $125,000 (R. 40). This latter figure was determined by deducting from the face amount of the then future installment payments a discount of approximately 6.348 percent per annum from the date of the death of S. C. McEachern to the average due date of the installments.

After the close of the evidence, both sides moved for a directed verdict. The District Court directed a verdict for petitioner. On appeal the Circuit Court of Appeals reversed, on the ground that the stipulation offered by respondent was admissible

and established a good defense, since it showed that in equity and good conscience petitioner was not entitled to recover.

SUMMARY OF ARGUMENT

The income on which petitioner erroneously paid taxes in 1929, 1930, and 1931, should have been reported and taxed in 1928 under Section 44 (d) of the Revenue Act of 1928. Since petitioner failed to report this income and pay a tax thereon in 1928, as required by law, and since the taxes so payable, but now uncollectible by reason of the statute of limitations, are greater than the taxes actually paid on the income, it would be inequitable to allow petitioner a recovery of the taxes paid. This is an action for money had and received, based on equitable principles, in which petitioner must show that respondent wrongfully withholds money equitably due petitioner. Where, as here, the money received by respondent, though received under a technical mistake in procedure under the revenue laws, was no greater than was justly due from petitioner as taxes on the income, no right of recovery in this form of action exists. *Stone* v. *White*, 301 U. S. 532. No violation of the statute of limitations results from the application of these equitable principles to this case.

In requiring the taxation of the income in 1928, Section 44 (d) is constitutional. It simply provides for the termination of the privileges granted by the installment basis of reporting income, when, because of the disposal by the taxpayer of the in-

stallment obligation, the continuance of those privileges would result in an avoidance of tax. Section 44 (d) does not tax that which is not income under the Sixteenth Amendment; it taxes the remaining portion of the profit realized by the taxpayer on the sale in which the installment obligation was received.

ARGUMENT

I

THE COURT BELOW CORRECTLY DECIDED THAT PETITIONER IN EQUITY AND GOOD CONSCIENCE IS NOT ENTITLED TO RECOVER

By Section 44 (d) of the Revenue Act of 1928 petitioner was required to report as income accruing to decedent in 1928, the year of death, the remaining portion of decedent's profit from the sale of the Industrial Life & Health Insurance Company stock in 1924. This petitioner failed to do. The return filed for 1928 made no mention of the installment obligation. While the amount of the payments on the obligation received during 1928 was included, this amount was stated as a separate sale in 1928 of fifty shares of the stock (R. 47). The additional tax legally payable by petitioner for 1928 on this unreported income is stipulated to be $11,625 (R. 47), no part of which petitioner has paid. Collection is now barred by the statute of limitations, and was barred at the time petitioner filed the claims for refund upon which this suit was brought.

Instead of reporting this income in 1928, petitioner, by mistake, reported it partially in each of the three returns filed on behalf of the estate for the years 1929, 1930, and 1931, and paid taxes thereon. The taxes so paid mistakenly, however, amounted to only $3,858.34, so that by reason of petitioner's mistake the Government has already lost $7,766.66 in revenue that was justly due. Petitioner now asks this Court for a return of the $3,858.34, which would free the income from all taxes whatsoever and would cause the Government to lose the entire $11,625 that should have been paid.

Under these circumstances we submit that the Circuit Court of Appeals correctly decided that the petitioner "ought not in good conscience" to recover, and that its judgment accordingly should be affirmed.[1] Respondent has not been unjustly enriched at the expense of petitioner. On the contrary, petitioner, through its own error, has already avoided payment of the greater part of the taxes justly due. In view of the equitable character of the petitioner's action, he should not be allowed to undo the payments actually made and escape taxation upon the transaction altogether.

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[1] The respondent in his answer to each count, after setting forth the facts and pleading that "it would be unconscionable for the plaintiff to be allowed any recovery from the defendant", asserted also that "plaintiff is estopped to assert and claim that any portion of the taxes in controversy in this action were not taxable to said estate * * *"

The decisions of this Court in *Stone* v. *White*, 301 U. S. 532; *Bull* v. *United States*, 295 U. S. 247; and *Lewis* v. *Reynolds*, 284 U. S. 281, among others, clearly support the conclusion of the Circuit Court of Appeals. This case, although arising on different facts, presents exactly the same equitable situation involved in *Stone* v. *White, supra*. There trustees had paid taxes which legally should have been paid by the beneficiary of the trust. Recovery of the taxes by the trustees was denied on the ground that the proceeds of recovery would inure to and unjustly enrich the beneficiary, and hence

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(R. 17, 18, 19, 20, 23, 24). The Circuit Court of Appeals, in holding that petitioner was not entitled to recover, said (R. 61):

"This is so not because of the existence of a technical estoppel or a waiver, but because his action was equitable in its nature and grounds, and he may not succeed in it unless he can show that the defendant has money which, *ex aequo et bono*, the defendant ought to refund."

The respondent does not now urge, as a distinct ground for affirming the judgment below, the existence in this case of a "technical estoppel." This is not, however, for the reasons advanced against such a contention in the brief for the petitioner.

The Commissioner did not here have "timely knowledge of all the material facts", as in the cases there relied upon. This Court will take judicial notice of the method of organization of the Bureau of Internal Revenue. *United States* v. *Jackson*, 104 U. S. 41. To charge the Government in the handling of income tax returns with the knowledge of the contents of estate tax returns would be pure fiction, and would require, if the Government wished to protect itself from misrepresentations and non-disclosures of fact subsequently revealed after the statute of limitations had run, the investigation of many thousands of returns now accepted

that the trustees could not show that they were equitably entitled to the money.

The action here is a suit against the collector for a refund of income taxes, as was the action in *Stone* v. *White*. All that was said there concerning the equitable nature of the proceeding as a successor of the common count in *indebitatus assumpsit* for money had and received is fully applicable here. It was there settled that no recovery could be had in this type of action without a showing that the defendant holds money to which the plaintiff is equitably entitled. To the same effect see *Lewis* v.

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without investigation for reasons of economy and public policy.

Nor is there room in this case for the contention that the Commissioner should have discovered the facts by his own investigation of the returns filed. The returns were doubly in error in selecting the wrong basis for determining gain upon the payments received, and in stating that the payments were received pursuant to a separate sale in the taxable year. It is sheer speculation to assert that inquiry into the first error would have disclosed the second. See Brief for the Petitioner, 21, 22.

The Commissioner's failure to collect the tax for 1928 under Section 44 (d) resulted plainly enough from the petitioner's failure to disclose the fact making for taxability—namely, the existence of an installment obligation. Doubt as to the existence of a technical estoppel arises only from the fact that petitioner's present case does not necessarily involve a reversal of his previous position that the payments were received pursuant to a separate sale. His recovery, accordingly, would not in strictness be defeated by an "estoppel" against denial of that earlier misrepresentation. The misrepresentation, on the other hand, together with the element of resulting unjust enrichment, is plainly ground for defense to an action equitable in character.

Reynolds, 284 U. S. 281, 283; *United States* v. *Jefferson Electric Co.,* 291 U. S. 386, 402; *Myers* v. *Hurley Motor Co.,* 273 U. S. 18, 24; *Crocker* v. *Malley,* 249 U. S. 223. As was said by this Court in *United States* v. *Jefferson Electric Co., supra* (pp. 402–403):

> This is often called an equitable action and is less restricted and fettered by technical rules and formalities than any other form of action. It aims at the abstract justice of the case, and looks solely to the inquiry, whether the defendant holds money, which *ex aequo et bono* belongs to the plaintiff.

The abstract justice of this case is identical with that of *Stone* v. *White, supra.* Here, as there, petitioner paid taxes on certain income in an erroneous manner under the technicalities of the tax laws, but the taxes paid were no more than were rightfully due on the income, and petitioner was in no way prejudiced by the error. In *Stone* v. *White* the tax was paid by the trustees when it should have been paid by the beneficiary, but no one was prejudiced since the tax in reality came from the beneficiary's funds. At bar the tax was paid on returns on behalf of the estate when it should have been paid on a return on behalf of the decedent, but no one is prejudiced since in either event payment comes from the same source, namely, the estate. Indeed, in this case, unlike *Stone* v. *White,* the tax-paying entity is identical.

The equity of respondent's position is not destroyed by the fact that the payments were made in different years from that in which they were legally due. It is a tax on the same income that is involved, and the erroneous dates of payment cannot affect the fact that the Government is entitled to retain a tax on that income. This is not a case where a separate barred tax liability on different income for a different year is sought to be applied to defeat refund of an overpayment of taxes on other income received during a later year. The taxes sought to be recovered here were paid on the income arising from the sale of stock by decedent in 1924, and the facts offered in evidence by respondent at the trial show that the taxes on *that income* have not been overpaid.

In this respect, the case resembles *Bull* v. *United States, supra,* in which the same interest had been treated erroneously, as a right to profits constituting capital passing at the decedent's death and subject to the estate tax, and subsequently had been correctly taxed as income received by the estate. This Court held the taxpayer entitled to recover so much of the income tax payment as duplicated the mistaken estate tax payment. "If the claim for income tax deficiency had been the subject of a suit", the Court said (p. 262), "any counter demand for recoupment of the overpayment of estate tax could have been asserted by way of defense and credit obtained * * *." Such a suit—save only

for the reversal of the parties—would have been almost the precise counterpart of this proceeding.

No violation of the statute of limitations results from the application of these equitable principles to deny a recovery by the petitioner. This is not a case, it should be emphasized, in which a barred tax liability is sought to be applied against a later mistaken payment on distinct income. As the Court said in *Stone* v. *White, supra* (301 U. S. at 538):

> The statutory bar to the right of action for the collection of the tax does not prevent reliance upon a defense which is not a set-off or a counterclaim, but is an equitable reason, growing out of the circumstances of the erroneous payment, why petitioners ought not to recover.

The payments for which petitioner is now suing were made before the falling of the bar of limitations applicable to the years for which the payments were made. The showing by which petitioner establishes that the income reported was not taxable in those years discloses that the income was taxable in another year for which it was not reported. In equity and good conscience, petitioner ought not to be able thus to undo a timely payment by a belated disclosure rendering it untimely.

The right of the Government under these circumstances to retain the money actually received may be taken as conclusively established by the decisions in *Stone* v. *White* and *Bull* v. *United States*,

supra, unless a single ground of distinction suggested by the petitioner affords a basis for differentiation. In *Stone* v. *White,* as the petitioner points out, the erroneous payment was made before collection on the correct basis had been barred. Conversely, in *Bull* v. *United States,* it appeared that the taxpayer's proper claim for refund could still have been asserted affirmatively at the time when the Government first proceeded against him on a correct theory of liability—although not at the time when the payment was made of which refund was sought. In the instant case all but $230.07 of the amount sued for was paid after the limitations period expired for the year 1928. We do not think that this circumstance is material; nor did the Court so treat it in the *Stone* and *Bull* cases. The Court in *Stone* v. *White,* citing a similar statement in the *Bull* case, said (p. 539):

> The government, by retaining the tax paid by the trustees, is not reviving a stale claim. Its defense, which inheres in the cause of action, is comparable to an equitable recoupment or diminution of petitioners' right to recover. "Such a defense is never barred by the statute of limitations so long as the main action is timely." *Bull* v. *United States,* 295 U. S. 247, 262 * * *.

In the *Stone* case, as here, the grounds upon which the Government's defense rested were not disclosed, and the defense was not asserted, until after the bar of the statute had fallen upon a claim

of affirmative liability.[2] To make the decision in that case turn upon the circumstance that the Government, had it had full information, might have attributed the payment to the correct liability, or might still have proceeded against the taxpayer upon that liability,[3] would be to emphasize an illusory opportunity, irrelevant to the broad equitable grounds upon which the Court's reasoning proceeded. No more in this case than in that is there undue danger to general principles of repose, for in no event can a defense be asserted which does not arise out of the same transaction with reference to which a timely suit is brought.

Petitioner's brief argues that the defense of "recoupment" is not open under the pleadings. The defense relied upon by the respondent, by whatever name called, was urged in both courts below and

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[2] In the *Bull* case, the taxpayer evidently learned of the Government's income tax claim before it was too late to file claim for refund of the estate tax payment. But this fact, if significant at all, weakens rather than otherwise the reasons for permitting recoupment.

[3] The opinion of the Court in *Stone* v. *White* refers to the circumstance of the time of the erroneous payment in the statement of facts (p. 533), but does not recur to it expressly in discussion of the problem. That circumstance, it should be pointed out, had a significance in the *Stone* case for which there is no parallel here. The erroneous payment had there been made in response to a deficiency assessed by the Commissioner. The time of the assessment was therefore evidence of the good faith of the Commissioner, serving to establish that "the government * * * [was] not reviving a stale claim" (p. 539).

was expressly made the ground of decision by the Circuit Court of Appeals (R. 61, 62). Petitioner did not contend in seeking a writ of certiorari that the court below had erred in deciding the case upon a ground not open on the record; and he may not so contend now. The respondent is accordingly free, under any view of the record, to take the position that the case was correctly decided upon the ground on which it was decided.

The defense in question, although in the nature of an equitable recoupment, is not strict recoupment but rests upon the necessity that the plaintiff in an action of this kind prove that he is justly and equitably entitled to the money he seeks. Respondent in this case was entitled to show any state of facts which would deny the equity of petitioner's claim, even if the answer went no further than a general plea of non-assumpsit, without resort to modern statutory authority for pleading equitable defenses in law actions. *Stone* v. *White, supra,* at 535. In *Lewis* v. *Reynolds, supra,* recovery was denied by reason of similar equitable principles, and the record in that case (No. 115, October Term, 1931) shows that the facts constituting the defense were not set up in the answer.

The defense here relied upon, however, was directly and unequivocally pleaded. The answer, in response to each count of the petition, sets up in detail the facts concerning the failure to report the income and pay a tax thereon in 1928, and con-

cludes that "it would be unconscionable for the plaintiff to be allowed any recovery from the defendant" (R. 16–20, 22–24). Plainly, on this state of the pleadings, the District Court erred in refusing to receive the evidence offered by the respondent concerning the year 1928. We submit that the court below correctly decided that under the facts in this case petitioner had not shown that respondent held money to which petitioner in equity and good conscience was entitled, and therefore had not made out a cause of action.

II

SECTION 44 (d) OF THE REVENUE ACT OF 1928 IS CONSTITUTIONAL

Respondent's defense to the claim of petitioner for refunds in this case is based on the failure of petitioner to report in the return for 1928, under the provisions of Section 44 (d) of the Revenue Act of 1928, the income which in part was thereafter erroneously reported for the years 1929, 1930, and 1931, and to pay a tax thereon for the year 1928 in an amount greater than that which has been paid in the later years. The ultimate answer which petitioner seeks to make to this defense is that Section 44 (d) of the Revenue Act of 1928 is unconstitutional.

Section 44 (d) is a part of what is known as the installment basis of accounting, whereby profits derived from installment sales are spread for tax-

ation over the period during which the installments are paid. The installment basis of accounting was considered and analyzed by this Court in *Burnet* v. *S. & L. Building Corp.*, 288 U. S. 406. It was there pointed out (p. 413) that prior to the Act of 1926 the Revenue Acts definitely recognized only two bases for tax returns: cash and accrual. Where sales were upon the installment plan, application of either of these bases led to hardship, payment of the total tax on ascertained profit often being required in a single year.[4] By regulations the Commissioner offered some alleviation, and the vendor was allowed to distribute the profit through the years during which purchase money was actually received.[5] The general principle underlying these regulations was to make division of the partial payments and apply part as return of capital and part to profit. In 1926 the Board of Tax Appeals disapproved all of the earlier regulations and pointed out that the statutes permitted returns only upon the cash or accrual basis.[6] Thereupon,

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[4] On realization of gain, see *McLaughlin* v. *Alliance Insurance Co.*, 286 U. S. 244, 249, *et seq.*

[5] Treasury Regulations 45, Art. 42, *infra*, pp. 40–41. For an exhaustive review of the history of installment sale regulations, see *Blum's, Inc.* v. *Commissioner*, 7 B. T. A. 737, 751, *et seq.*

[6] *B. B. Todd, Inc.* v. *Commissioner*, 1 B. T. A. 762, decided March 16, 1925. See also *H. B. Graves Co.* v. *Commissioner*, 1 B. T. A. 859; *Hoover-Bond Co.* v. *Commissioner*, 1 B. T. A. 929, and *650 West End Avenue Co.* v. *Commissioner*, 2 B. T. A. 958.

Congress enacted Section 212 (d) of the Revenue Act of 1926, *infra,* pp. 37–38. The end in view was to permit the Commissioner to make assessments according to the general principle theretofore followed under regulations deemed appropriate to the varying situations. The new plan was optional. Taxpayers were allowed to elect whether to make returns under the regulations upon the new basis or upon one of the old bases.

Subsequently to the enactment of Section 212 (d) of the Revenue Act of 1926, considered by this Court in *Burnet* v. *S. & L. Building Corp., supra,* it was discovered that the extension of this privilege to taxpayers resulted in the possibility of widespread loss of revenue in the event of a disposition by the vendor of the obligations. Upon such a disposition, as, for example, a transmission of the obligation upon the death of the vendor, the person receiving the obligation would have an entirely new basis upon which to report the payments received from it for income tax purposes. This basis would be the fair market value of the obligation at the time of the transfer. *Brewster* v. *Gage,* 280 U. S. 327. Therefore, any portion of the profit received by the original vendor upon the sale, which under the privilege of installment reporting was not taxed prior to the vendor's death, would remain entirely untaxed.

To remedy this situation, Congress, in reenacting Section 212 (d) as Section 44 (b) of the Revenue

Act of 1928, added a further provision, which is Section 44 (d) of the Revenue Act of 1928, now in issue. Section 44 (d) provided:

> If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and (1) in the case of satisfaction at other than face value or a sale or exchange—the amount realized, or (2) in case of a distribution, transmission, or disposition otherwise than by sale or exchange—the fair market value of the obligation at the time of such distribution, transmission, or disposition. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full.

This statute taxes the remaining unreported profit on the sale in the year in which the vendor disposes of the obligations by transmission at death or otherwise. The unreported profit remaining, which is taxed, is computed under the statute as being the fair market value of the obligation at the time of disposal (in the case of transmission at death), less the amount of the original cost basis of the property which has not yet been utilized by the taxpayer in computing profits on earlier installments. The effect of this section, then, is to terminate the privilege of spreading the profit over

a period of years, which is given by the installment method, in any case where the continuation of that privilege would result in the avoidance of taxes on part of the income.

No court that has considered the constitutionality of Section 44 (d) has thought it invalid. On the contrary, the constitutionality of the section has been directly upheld by five Circuit Courts of Appeals, including the court below, and by the Court of Claims. *Lawlor* v. *Commissioner,* 78 F. (2d) 567 (C. C. A. 9th); *Crane* v. *Helvering,* 76 F. (2d) 99 (C. C. A. 2d); *Nuckolls* v. *United States,* 76 F. (2d) 357 (C. C. A. 10th); *Williams* v. *Commissioner,* 79 F. (2d) 518 (C. C. A. 3d); *Provident Trust Co. of Philadelphia* v. *Commissioner,* 76 F. (2d) 810 (C. C. A. 3d); *Moore* v. *United States,* 10 F. Supp. 143 (C. Cls.).

The attack here made on the validity of this section is that it lays a tax on the transmission of installment obligations at death and that such transmission does not result in any income constitutionally taxable under the Sixteenth Amendment. The error in this argument, we submit, is that this section does not and was not intended to tax any purported income arising from the transmission of the obligation at death. The income taxed is the income received by the vendor by reason of the sale transaction. Because of the action of the vendor in choosing to avail himself of the privilege of the installment basis, the vendor was permitted to re-

port this profit piecemeal over a number of years. When, upon the vendor's death, it became no longer possible to tax him in the manner contemplated by the installment basis, the Congress through Section 44 (d) terminated the privilege granted him, and required the remaining portion of the income arising from the sale to be then reported and taxed.

Congress has clearly indicated that, in enacting Section 44 (d), its purpose was to tax the remaining unreported income which had arisen from the prior installment sale. The Ways and Means Committee of the House of Representatives, in reporting the Revenue Act of 1928, said with regard to Section 44 (d) (H. Rep. No. 2, 70th Cong., 1st Sess., pp. 14, 16):[7]

> *Gain or loss upon Disposition of Installment Obligations.*—Subsection (d) contains new provisions of law to prevent evasion of taxes in connection with the transmission of installment obligations upon death, their distribution by way of liquidating or other dividends, or their disposition by way of gift, or in connection with similar transactions. The situations above specified ordinarily do not give rise to gain and yet at the same time it is urged that they permit the recipient to obtain a greatly increased basis in his hands for the property received, except in the case of gifts. It therefore seems desirable to clarify the matter. The installment basis accords the taxpayer *the*

[7] Set out in full, Appendix, *infra*, pp. 46–47.

> *privilege of deferring* the reporting at the time of sale of the gain realized, until such time as the deferred cash payments are made. To prevent the evasion the subsection *terminates the privilege of longer deferring the profit* if the seller at any time transmits, distributes, or disposes of the installment obligations and compels the seller at that time to report the *deferred profits.* [Italics supplied.]

Moreover, that Congress intended by Section 44 (d) to terminate the privilege of reporting the income from the sale on the installment basis and to tax the remaining portion of that income is indicated by the amendment to Section 44 (d) of the 1928 Act, which was incorporated in the section as it appeared in the Revenue Act of 1932.[8] That amendment was as follows:

> SEC. 44. INSTALLMENT BASIS.
>
> (d) *Gain or Loss upon Disposition of Installment Obligations.*—* * * This subsection shall not apply to the transmission at death of installment obligations if there is filed with the Commissioner, at such time as he may by regulation prescribe, a bond in such amount and with such sureties as he may deem necessary, conditioned upon the return as income, by the person receiving

[8] That this amendment may properly be considered, see *Helvering* v. *Twin Bell Oil Syndicate*, 293 U. S. 312. Cf. *W. A. Sheaffer Pen Co.* v. *Lucas*, 41 F. (2d) 117, 119 (App. D. C.); *United States* v. *Freeman*, 3 How. 556, 564.

> any payment on such obligations, of the same proportion of such payment as would be returnable as income by the decedent if he had lived and had received such payment.

This amendment was proposed for reasons explained to Congress by the Senate Committee on Finance, as follows (S. Rep. No. 665, 72d Cong., 1st Sess., p. 21):

> Your committee has added to Section 44 (d) a provision that the subsection shall not apply to the transmission at death of installment obligations if a bond is filed in the proper amount conditioned upon the return as income by any person receiving any payment on account of such obligations of the same proportion of such payment as would have been returnable by the decedent had he lived and received the same. * * *

And in explanation of the action of the House conferees in receding from their objection to the amendment, the conference report stated (H. Rep. No. 1492, 72d Cong., 1st Sess., p. 13):

> Amendment No. 38: The existing law required, in the case of installment obligations transmitted at death, that there be included as income in the return of the decedent for the year of his death the unreturned profit represented by such obligations. This amendment eliminates such requirement if there is filed with the commissioner a bond conditioned upon the return as income, by the person receiving any payment on such

> obligations, of the same proportion of such payment as would be returnable as income by the decedent had he lived and received the same. The House recedes.

It is clear from this legislative history that Congress intended not to tax some new income purporting to have arisen by the transmission of the installment obligation at death, but rather intended to prevent an avoidance of taxes, which otherwise would have resulted from the extension of the privilege of the installment basis.

Petitioner in his brief does not seem to challenge the power of Congress to legislate for this purpose. Petitioner contends, however, that the operation of Section 44 (d) may not always be confined to taxing income theretofore received and unreported, but that it may tax as income what is merely appreciation in value.

1. It would seem to be a sufficient answer to this contention to point out that it does not appear that such a result will follow from the application of the statute in this case. The parties have stipulated (Defendant's Exhibit A, R. 46–48) that if the gain or profit on the $150,000 in installment obligations unpaid at the date of death had been included in the return for 1928, as provided by Section 44 (d), an additional tax would have been disclosed in the sum of $11,625. As an alternative to the installment basis, the petitioner's decedent was taxable, in 1924 alone, upon the cash received plus the fair market value of the purchase money obli-

gations, less cost.[9] Revenue Act of 1924, Sec. 202 (c), 43 Stat. 253. With respect to the $150,000 of unpaid obligations here in question, accordingly, he would have been taxable on the fair market value less $2,500—the unutilized balance of cost. The record is barren of evidence to show that the tax in 1924, so computed, would have been less than the $11,625 here stipulated to be due.

2. Petitioner's argument, however, is built upon a basic misapprehension which ought not to be permitted to go without a direct answer. Application of Section 44 (d) to the fair market value of the unpaid obligations at date of death ($125,000), as seemingly required by its terms, would not have constituted taxation of unrealized income in violation of the Sixteenth Amendment. This is so even though that fair market value—which does not directly appear here—exceeded the fair market value at date of sale.

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[9] The petitioner in his brief (pp. 13, 14) concedes that this would be the applicable method of taxation if the purchase money obligations had been represented by negotiable promissory notes. See also the illustrative case in Appendix B, p. 48. There is no basis in the Constitution, or in the statutes, or in the practice of the Bureau of Internal Revenue, for the suggestion that this method of treating the fair market value of obligations received as the equivalent of cash must be confined to the case of negotiable notes. Cf. *United States* v. *Phellis*, 257 U. S. 156. The only relevant question is whether the purchase money obligations in fact have a fair market value. The record does not show that the obligation in this case did not have such a value in 1924. That it did is clearly to be inferred from the stipulated fact that the balance of the obligation in 1928 had a fair market value of $125,000 (R. 40).

The fair market value of an installment obligation may increase between the time of sale and the time of death for either or both of two reasons: first, because the obligation does not bear interest and the amount of the discount decreases as maturity approaches; and, second, because the credit of the obligor, being first at a discount, subsequently improves. The first situation is the only one which may conceivably be said to be presented on this record.[10] Both situations, however, are similar in principle; and in neither is the constitutionality of the section, in its ordinary operation, open to question.

The argument for the petitioner confuses problems of accounting method with issues of the realization of income under the Sixteenth Amendment. Accretions in the value of installment obligations subsequent to the date of contract are akin only in exceptional cases to accretions, for example, in the value of land occurring subsequently to its acquisition. The latter are unrelated to the original transaction and independent of it. With respect to them, no taxable event occurs until the land again changes hands. Accretions in the value of installment obligations, on the other hand, grow out of the original agreement, and frequently, as in

[10] The installments in fact had been paid when due. The balance outstanding was recognized in 1928 to be subject only to a discount of 6.348—attributable clearly to the absence of interest (R. 40). There is no evidence whatever that discount for any additional factor would have been appropriate in 1924.

the case of a non-interest-bearing obligation, are precisely responsive to its terms. With respect to profits on the transaction, a taxable event occurs not only at the time of the original agreement but whenever a periodical payment is made. Within broad limits, therefore, the problem is simply one of fair allocation of the cost to be allowed and the gain to be recognized at the time of each payment. The inappropriateness of an attempt to make this allocation conform to a rigid and technical pattern was pointed out by this Court in *Burnet* v. *S. & L. Building Corp., supra.*

Had the petitioner's decedent not elected in 1924 to be taxed upon the installment basis, he would have paid a tax at the capital gain rate upon the sum of the cash payment received and the then market value of the entire unpaid purchase money obligation, less cost. Revenue Act of 1924, Section 202 (c), 43 Stat. 253. That market value would have been determined, in the absence of any question affecting the credit of the maker, by deducting from the face value an appropriate discount from the due dates of the installment payments to the date of sale. The market value, whether or not reflecting any further discount, would have constituted the new basis of the obligation. That portion of each later payment representing an excess over the basis allocable to such payment would have been taxable in later years at the applicable individual normal and surtax rates. Such of those

later taxes as would have fallen due before death must, of course, be taken into account in comparison of the gains taxable upon the installment basis and those taxable upon the normal basis.[11]

The result of such a comparison—so far as the interest factor is concerned—turns upon the method which would have been employed, in taxation on the normal basis, in determining the discounted market value in 1924, and the corresponding method for "recovering" the discount for recognition as income in later years. If each payment were discounted separately from the date of sale to the due date of that payment, and, when the payment was made, only the amount of the discount for that payment recognized as income, then

[11] It is not to be implied from the making of this concrete comparison that taxation under Section 202 (c) of the Revenue Act of 1924 and corresponding provisions of other acts marks the limits of Congressional power. Taxation on the accrual basis, common in the installment business, of course, involves anticipation to much greater degree of actual receipt in cash. The petitioner's decedent elected to be taxed under a remedial statute (Sec. 212 (d) of the Revenue Act of 1926) which fixed as the profit to be taxed the amount "to be realized", that is, the face of the obligation. Fair market value at date of sale has no place, then, in measuring the validity of Section 44 (d). In this situation there was an unreported profit of $147,500 at the time of decedent's death. The amount that could have been taxed under Section 44 (d), under the agreed facts, is $122,500, which eliminates any appreciation to be realized on the face of the unpaid installment obligations involved herein. Congress may constitutionally lay down any measure it sees fit, and certainly any reasonable measure, in a remedial statute which is applicable only upon the election of the taxpayer.

the taxable gains recognized on the normal basis up to and including 1928 would evidently have been less than those recognized on the installment basis through the application of Sections 44 (b) and 44 (d). For, in that case, no gain would have been recognized during the decedent's lifetime upon that portion of the payments falling due after 1928 reflecting the discount upon those payments from the date of sale to 1928. But this differential would merely be a differential incident to a different method of accounting and not, as the petitioner's argument implies, one critical to the power of Congress under the Sixteenth Amendment. Alternatively the discount might have been computed by applying a fixed percentage to the entire unpaid obligation, and "recovering" accordingly as income in later years the same percentage of each installment payment. Under this method, the gain recognized before the decedent's death would probably have been somewhat less (depending upon the percentage used) than that recognized under Sections 44 (b) and 44 (d). But once again, this circumstance is not material to any issue of constitutional power. There remains a third method of determining the proportion of the original discount to be allocated to each payment, which so far as appears would in fact have been followed by the Bureau of Internal Revenue, and under which the total gains recognized would have exactly equalled the gains recognized on the in-

stallment basis through the application of Sections 44 (b) and 44 (d).[12] By this method the taxpayer would have been regarded as recovering as income in 1925, for example, that proportion of the $30,000 payments for that year reflecting the discount upon the entire debt of $270,000 outstanding in that year. Similarly, the payment in 1926 would be regarded as constituting income to the extent of the discount for the entire debt of $240,000 outstanding in the second year. The effect of Section 44 (d)—so far as the interest factor is concerned—is to follow precisely this method. For this method at the end of 1928 would have left the seller untaxed only on the amount of subsequent payments reflecting the discount to 1928 on the debt then outstanding. It is stipulated in this case (R. 40) that the market value of $125,000 in 1928 was determined by discounting to 1928 the payments then outstanding, leaving the seller similarly untaxed to the extent of this discount.

Further discounts in order to determine market value at time of sale, attributable to other factors than the absence of interest, raise no problem importantly different. Like the discount just considered, they will be reflected, when no longer justified, in taxable gains subsequently recognized; and

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[12] Appendix B, *infra*, p. 48, presents in tabular form a comparison between the gain recognized under Sections 44 (b) and 44 (d) and the gain which would be recognized in taxation on the normal basis under each of the three methods described in the text for computing the discount.

the precise time of their recognition is a question of accounting not touching consfitutional power. As each installment payment falls due, taxation on the normal basis might recognize—for reasons of administrative convenience—only an aliquot portion of any increase in the value of the entire obligation. But surely it would be competent for Congress to tax a greater proportion of the earlier payments by allocating to later payments more than their aliquot share of cost.[13] This is in effect what Section 44 (d) does in recognizing the entire increase. The disadvantage of this recognition, moreover, is counterbalanced by the advantage to the taxpayer in the event of *decrease* in market value between the time of sale and the time of death.

Petitioner's argument assumes a degree of exactitude in the concept of realization of income seldom attributed to it. The assumption will not survive examination. It is evident that different methods of accounting for gains and losses upon installment sales are possible and legitimate; and that the difference in method will affect not only the amount of gain recognized at the inception of the transaction but the precise period of recognition of later gain. In an income tax world of shifting rates and schedules there can be no assurance that the ultimate tax paid upon a given transaction

[13] Special circumstances, of course, might be presented—i. e., an unusually low original discount—in which the amount of any year's payment would set a limit upon the amount of gain to be recognized in that year.

according to one method will precisely equal the tax paid according to another. As in the examples just considered, part of the gain may be taxed at the capital gain rate, while the rest is subjected to the varying individual or corporate normal income and surtax rates. So far as a balance can be struck, from the point of view of the taxpayer, the advantage in ordinary course would appear to be with the installment method. That method—made available as a privilege which might have been withheld—permits postponement of a burdensome weight of taxation which otherwise would be incurred at the outset of an installment transaction. Under Section 44 (d) of the 1928 Act, it has the further advantage—equalled by no other method—of affording the taxpayer protection against *diminution* of the value of the obligation.

Apart from this feature of Section 44 (d), which works in favor of the taxpayer, the installment method under the 1928 Act furnished double assurance to the Government that all profit received on installment transactions would be taxed and to the taxpayer that no greater amount would be taxed.[14] Petitioner's argument seeks to destroy the harmony of this statutory scheme. Its acceptance would result, in circumstances like those of the case at bar, in the escape of substantial profits from any taxation whatsoever. Beyond question, as two Circuit Courts of Appeals have decided—when to

[14] See Appendix B, *infra*, p. 48.

decide more was unnecessary, Section 44 (d) is valid as applied to transactions occurring after its enactment.[15] The reasoning of those decisions will be seen, upon consideration, to be applicable to transactions before as well as after. For petitioner's decedent, in electing the installment basis, did not elect a static method of taxation. Since 1924 the installment method has been expressly validated by Congress, and its details have been altered in various respects to the benefit of the taxpayer. The 1932 amendment removes a final hardship to the taxpayer by permitting the representatives of a decedent to avoid a large lump sum payment in a later year, as the installment method itself permitted the decedent to avoid it in the year of the contract. Taxpayers electing the installment basis have had the advantage of these modifications upon their enactment. They ought not to be permitted to escape the operation of a further modification designed to prevent large amounts of profit, which in the absence of the election might have been taxed, from going untaxed altogether.

CONCLUSION

We conclude that petitioner was constitutionally required by Section 44 (d) of the Revenue Act of 1928 to pay a tax in 1928 on the remaining income from the installment sale, and that the court below correctly held that the District Court erred in re-

[15] *Crane* v. *Helvering*, 76 F. (2d) 99 (C. C. A. 2d); *Nuckolls* v. *United States*, 76 F. (2d) 357 (C. C. A. 10th).

fusing to receive evidence establishing, as a defense to the present suit, the failure of petitioner to report the income and pay the tax thereon.

Respectfully submitted.

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OCTOBER 1937.

APPENDIX A

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 202.

* * * * *

(c) The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

* * * * *

SEC. 212.

* * * * *

(d) Under regulations prescribed by the Commissioner with the approval of the Secretary, a person who regularly sells or otherwise disposes of personal property on the installment plan may return as income therefrom in any taxable year that proportion of the installment payments actually received in that year which the total profit realized or to be realized when the payment is completed, bears to the total contract price. In the case (1) of a casual sale or other casual disposition of personal property for a price exceeding $1,000, or (2) of a sale or other disposition of real property, if in either case the initial payments do not exceed one-fourth of the purchase price, the income may, under regulations prescribed by the Commissioner with the approval of the Secretary, be returned on the basis and in the manner above prescribed in this subdivision. As used in this subdivision, the term "initial payments" means the payments received in cash or property other than evi-

dences of indebtedness of the purchaser during the taxable period in which the sale or other disposition is made.

SEC. 1208. The provisions of subdivisions (d) of section 212 shall be retroactively applied in computing income under the provisions of the Revenue Act of 1916, the Revenue Act of 1917, the Revenue Act of 1918, the Revenue Act of 1921, or the Revenue Act of 1924, or any of such Acts as amended. Any tax that has been paid under such Acts prior to the enactment of this Act, if in excess of the tax imposed by such Acts as retroactively modified by this section, shall, subject to the statutory period of limitations properly applicable thereto, be credited or refunded to the taxpayer as provided in section 284.

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 44. INSTALLMENT BASIS.

(a) *Dealers in personal property.*—Under regulations proscribed by the Commissioner with the approval of the Secretary, a person who regularly sells or otherwise disposes of personal property on the installment plan may return as income therefrom in any taxable year that proportion of the installment payments actually received in that year which the gross profit realized or to be realized when payment is completed, bears to the total contract price.

(b) *Sales of realty and casual sales of personalty.*—In the case (1) of a casual sale or other casual disposition of personal property (other than property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year), for a price exceeding $1,000, or (2) of a sale or other disposition of real

property, if in either case the initial payments do not exceed 40 per centum of the selling price, the income may, under regulations prescribed by the Commissioner with the approval of the Secretary, be returned on the basis and in the manner above prescribed in this section. As used in this section the term "initial payments" means the payments received in cash or property other than evidences of indebtedness of the purchaser during the taxable period in which the sale or other disposition is made.

* * * * *

(d) *Gain or loss upon disposition of installment obligations.*—If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and (1) in the case of satisfaction at other than face value or a sale or exchange—the amount realized, or (2) in case of a distribution, transmission, or disposition otherwise than by sale or exchange—the fair market value of the obligation at the time of such distribution, transmission, or disposition. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full.

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 44. INSTALLMENT BASIS.

* * * * *

(d) *Gain or Loss upon Disposition of Installment Obligations.*—* * * This subsection shall not apply to the transmission at death of installment obligations if there is

filed with the Commissioner, at such time as he may by regulations prescribe, a bond in such amount and with such sureties as he may deem necessary, conditioned upon the return as income, by the person receiving any payment on such obligations, of the same proportion of such payment as would be returnable as income by the decedent if he had lived and had received such payment.

Treasury Regulations 45:

ART. 42. *Sale of personal property on installment plan.*—Dealers in personal property ordinarily sell either for cash, or on the personal credit of the buyer, or on the installment plan. Occasionally a fourth type of sale is met with, in which the buyer makes an initial payment of such a substantial nature (for example, a payment of more than 25 per cent) that the sale, though involving deferred payments, is not one on the installment plan. In sales on personal credit, and in the substantial payment type just mentioned, obligations of purchasers are to be regarded as the equivalent of cash, but a different rule applies to sales on the installment plan. Dealers in personal property who sell on the installment plan usually adopt one of four ways of protecting themselves in case of default: (*a*) Through an agreement that title is to remain in the seller until the buyer has completely performed his part of the transaction; (*b*) by a form of contract in which title is conveyed to the purchaser immediately, but subject to a lien for the unpaid portion of the purchase price; (*c*) by a present transfer of title to the purchaser, who at the same time executes a reconveyance in the form of a chattel mortgage to the seller; or (d) by conveyance to

a trustee pending performance of the contract and subject to its provisions. The general purpose and effect being the same in all of these plans, it is desirable that a uniformly applicable rule be established. The rule prescribed is that in the sale or contract for sale of personal property on the installment plan, whether or not title remains in the vendor until the property is fully paid for, the income to be returned by the vendor will be that proportion of each installment payment which the gross profit to be realized when the property is paid for bears to the gross contract price. Such income may be ascertained by taking as profit that proportion of the total cash collections received in the taxable year from installment sales (such collections being allocated to the year against the sales of which they apply), which the annual gross profit to be realized on the total installment sales made during each year bears to the gross contract price of all such sales made during that respective year. In any case where the gross profit to be realized on a sale or contract for sale of personal property has been reported as income for the year in which the transaction occurred, and a change is made to the installment plan of computing net income, no part of any installment payment received subsequent to the change, representing income previously reported on account of such transaction, should be reported as income for the year in which the installment payment is received; the intent and purpose of this provision is that where the entire profit from installment sales has been included in gross income for the year in which the sale was made, no part of the installment payments received subsequently on account

of such previous sales shall again be subject to tax for the year or years in which received. Where the taxpayer makes a change to this method of computing net income his balance sheet should be adjusted conformably. If for any reason the vendee defaults in any of his installment payments and the vendor repossesses the property, the entire amount received on installment payments, less the profits already returned, will be income of the vendor for the year in which the property was repossessed, and the property repossessed must be included in the inventory at its original cost to himself, less proper allowance for damage and use, if any. If the vendor chooses as a matter of consistent practice to treat the obligations of purchasers as the equivalent of cash, such a course is permissible.

Treasury Regulations 74:

ART. 355. *Gain or loss upon disposition of installment obligations.*—If an installment obligation is satisfied at other than its face value or is sold or exchanged, gain or loss results to the extent of the difference between (1) the excess of the face value of the obligation over the amount of income which would be returnable were the obligation satisfied in full and (2) the amount realized upon such disposition.

If an installment obligation is distributed, transmitted, or disposed of otherwise than by sale or exchange, gain or loss results to the extent of the difference between (1) the excess of the face value of the obligation over the amount of income which would be returnable were the obligation satisfied in full and (2) the fair market value of the obligation at the time of such distribution, transmission, or disposition.

The entire amount of gain or loss resulting from the disposition or satisfaction of installment obligations shall be recognized except as provided in section 112 and articles 571–580.

Example (1): In 1928 the M Corporation sold a piece of real estate to B for $20,000. The company acquired the property subsequent to February 28, 1913, at a cost of $10,000. During 1928 the company received $5,000 cash and the vendee's notes for the remainder of the selling price, or $15,000, payable in subsequent years. Before the vendee made any further payments the company sold the notes for $13,000 in cash. The company derived taxable income in the amount of $5,500 from the sale of the notes, computed as follows:

Proceeds of sales of notes		$13,000
Selling price of property	$20,000	
Cost of property	10,000	
Total profit to be realized when property is paid for	10,000	
Total contract price	20,000	
Percent of profit, or proportion of each payment returnable as income, $10,000 divided by $20,000, 50 percent.		
Face value of notes	15,000	
Amount of income returnable were the notes satisfied in full, 50 percent of $15,000	7,500	
Excess of face value of note over amount of income returnable were the notes satisfied in full		7,500
Taxable income derived from sale of notes		5,500

Example (2): Suppose in the example given above the M Corporation, instead of selling the notes, distributed them to its shareholders as a dividend, and at the time of such distribution the fair market value of the notes was $14,000. The company would derive taxable income in the amount of $6,500 from such disposition of the notes, computed as follows:

Fair market value of notes	$14,000
Excess of face value of notes over amount of income returnable were the notes satisfied in full (computed as in example (*l*))	7,500
Taxable income derived from disposition of notes	6,500

S. Rep. No. 52, 69th Cong., 1st Sess., p. 19:

Section 212 (d): The revenue act of 1924 and prior acts have specifically provided two bases only for reporting income—first, cash receipts and disbursements, and, second, accrual. Since the enactment of the revenue act of 1921, however, section 202 (f) and its successors have impliedly recognized the existence of a third basis, the installment basis, without in any wise defining the situations and businesses to which such basis might be applied. The Commissioner of Internal Revenue has in his regulations provided, in pursuance of his authority to require a method of computation that will clearly reflect income, the installment basis for reporting income in certain cases. For instance, Regulations 65, as issued under the revenue act of 1924, provides that all dealers in personal property sold on the installment plan, whether or not title remains in the vendor until payment is completed, may return as income that proportion of the total cash collections received in the taxable year from installment sales which the annual gross profits on the total sales made during each year bear to the gross contract prices of all such sales. Vendors in isolated sales of personal property or in sales of real property on deferred-payment plans may return as income as of the year of actual receipt that proportion of each payment which the profit upon completion of all payments bears to the contract price, subject to the limitation, however, that the initial pay-

ment must not exceed 25 per centum of the contract price.

However, recent decisions of the Board of Tax Appeals (see appeal of 650 West End Ave. Co., appeal of Manomet Cranberry Co., and appeal of B. B. Todd (Inc.)—all decided during the past year) have held that similar regulations under earlier acts were invalid and that the commissioner under the law could authorize no basis other than the cash receipts and disbursements basis or the accrual basis, except for certain minor departures. The committee amendment, in order to meet the situation resulting from the decisions, places the principles of the commissioner's regulations in the law and thereby validates the regulations for all periods after January 1, 1925.

Deferred-payment contracts other than installment contracts are not affected by the committee amendment. When the initial payment exceeds 25 per cent of the price in the case of an isolated sale of personal property, or in the case of sales of real property, the obligations that are received in addition to the initial payment are to be regarded as the equivalent of cash if such obligations have a fair market value. In consequence that portion of the initial payment and of the fair market value of such obligations which represents profit is to be returned as income as of the taxable year of the sale.

The application of the installment basis as provided in the committee amendment should eliminate necessity for appraisals of the obligations of the purchaser in deferred-payment sales, as required under the Board of Tax Appeals decisions, save in those cases where, because of a large initial payment, i. e., one in excess of 25 per cent of the price,

the property sold and serving as security for the unpaid balance has a value adequate to give the obligations a market value.

H. Rep., No. 2, 70th Cong., 1st Sess., p. 16:

Gain or Loss upon Disposition of Installment Obligations.—Subsection (d) contains new provisions of law to prevent evasion of taxes in connection with the transmission of installment obligations upon death, their distribution by way of liquidating or other dividends, or their disposition by way of gift, or in connection with similar transactions. The situations above specified ordinarily do not give rise to gain, and yet at the same time it is urged that they permit the recipient to obtain a greatly increased basis in his hands for the property received, except in the case of gifts. It therefore seems desirable to clarify the matter. The installment basis accords the taxpayer the privilege of deferring the reporting at the time of sale of the gain realized until such time as the deferred cash payments are made. To prevent the evasion the subsection terminates the privilege of longer deferring the profit if the seller at any time transmits, distributes, or disposes of the installment obligations and compels the seller at that time to report the deferred profits. The subsection also modifies the general rule provided in subsection (a) for the ascertainment of the percentage of profit in the deferred payments, in those cases in which the obligations are satisfied at other than their face value or are sold or exchanged. The modification permits a compensating reduction in the percentage of profit in case the obligations are satisfied

at less than their face value, or are sold or exchanged at less than face value.

* * * * * *

S. Rep. No. 665, 72d Cong., 1st Sess., p. 21:

SECTION 44 (d). TRANSMISSION AT DEATH OF INSTALLMENT OBLIGATIONS.

Your committee has added to section 44 (d) a provision that the subsection shall not apply to the transmission at death of installment obligations if a bond is filed in the proper amount conditioned upon the return as income by any person receiving any payment on account of such obligations of the same proportion of such payment as would have been returnable by the decedent had he lived and received the same. It has come to the attention of your committee that considerable hardship sometimes occurs in the application of existing law to cases of decedents who die possessed of substantial amounts of installment obligations. In such cases the entire amount of the profit represented by the obligations must be reported as income in the return of the decedent for the year of his death. Your committee believes that if, for example, the estate of the decedent or his next of kin or legatees file a bond to return as income the proper proportion of the payments received by them on account of the installment obligations received from the decedent, the revenue will be properly protected. This section is accordingly amended to provide for such procedure.

APPENDIX B

Taxation of gains upon sale of stock costing $5,000 for $300,000—$30,000 down payment and nine annual installment payments of $30,000 each

Year taxable	Description of payment		Installment basis, R. A. 1928, § 44	Normal basis, R. A. 1924, § 202 (c), flat rate of discount	Normal basis, R. A. 1924, § 202 (c), discounting each payment separately	Normal basis, R. A. 1924, § 202 (c), discounting whole outstanding debt for each year
1924	Sales price, cash	$30,000.00				
	Market value of obligation	200,994.65				
	Total	230,994.65				
	Less: Cost	5,000.00				
				$225,994.65	$225,994.65	$225,994.65
1924	Down payment	30,000.00	$29,500.00			
1925	Installment payment	30,000.00	29,500.00	7,667.26	1,790.87	12,757.29
1926	Installment payment	30,000.00	29,500.00	7,667.26	3,474.69	11,664.85
1927	Installment payment	30,000.00	29,500.00	7,667.26	5,058.01	10,500.93
1928	Installment payment	30,000.00	29,500.00	7,667.26	6,546.82	9,263.13
	Commuted value of remaining obligations, assuming that death of taxpayer occurred December 31, 1928	125,182.85				
	Less: Unrecovered cost	2,500.00				
			122,682.55			
	Profit taxable to taxpayer		270,182.85	254,663.69	242,865.04	270,182.85

	Profit Taxable to Taxpayer's Estate				
1929	Discount fifth installment	7,946.76	4,963.43	1,790.87	7,946.76
1930	Discount sixth installment	6,546.82	4,963.43	3,474.69	6,546.82
1931	Discount seventh installment	5,058.01	4,963.43	5,058.01	5,058.01
1932	Discount eighth installment	3,474.69	4,963.43	6,546.82	3,474.69
1933	Discount ninth installment	1,790.87	4,963.43	7,946.76	1,790.87
	Profit taxable to estate	24,817.15	24,817.15	24,817.15	24,817.15
	Total	295,000.00	279,480.84	267,682.19	295,000.00

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1937

No. 6

D. W. McEACHERN, ADMINISTRATOR OF THE ESTATE OF S. C. McEACHERN, DECEASED,

Petitioner,

vs.

J. T. ROSE, FORMER COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

BRIEF OF AMICUS CURIÆ.

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BRIEF OF AMICUS CURIÆ.

Comes now, Robert Ash, as *Amicus Curiæ,* and presents this brief directed to the decisions of this Court on the question of equity in the interpretation of taxing statutes.

The brief is submitted because it appears to the writer that the decisions of this Court with reference to the nature of a taxpayers right of action to recover overpayments of taxes are conflicting, and that the Court's tendency at times to

analogize the action to an action for money had and received, equitable in nature, is most dangerous to the orderly administration of the Federal tax laws. A brief review of the authorities will make it clear that if any such principle has been announced by this Court in any case, a contrary principle has been followed in other cases and should be followed in all cases.

Whatever may be the origin of the action to recover taxes overpaid and whatever may be the common law restriction upon an action for money had and received, it is clear that the present suit is an action to recover amounts, the refund of which is expressly commanded by statute, and that it is only necessary, as in any other legal action to enforce a statutory right, to show that the statute requires the payment of money—not to show that in equity and good conscience plaintiff is entitled to the money. It may be that a common law right would subsist if Congress should take away the statutory right, but so long as the statutory right expressly given by Congress remains, equity is not a matter of importance.

This Court in *Bull* v. *United States,* 295 U. S. 247, 15 A. F. T. R. 1069, truly expressed the nature of the action to recover taxes overpaid. It said that the action is essentially one by the Government to test the correctness of the summary collection which for reasons of public policy it must be permitted to make before its legal right to the money is tested. It says that the taxpayer in such a suit is not really a plaintiff, but that he is actually a defendant and as such can plead recoupment. This holding was essential to the result reached in the *Bull* case. If the taxpayer is a defendant in such a suit, where he is clearly entitled to rely upon all his legal defenses, by what magic could he be converted in the present suit into a plaintiff in an action *ex aequo et bono?*

In *Jefferson Electric Company* v. *United States,* 291 U. S. 386, 13 A. F. T. R. 866, this Court upheld the right of

Congress to restrict recovery in cases where the tax had been collected from another. In sustaining the Congressional restrictions, the Court relied upon the fact that the statute prevented the taxpayer from recovering only when in justice and equity he was not entitled to the recovery. The Court clearly admitted, however, that before the Congressional restriction, recovery would have been granted in the suit.[1] If an action to recover taxes overpaid were available only when in justice and equity the taxpayer was entitled to recover, no Congressional restriction would be required to prevent recovery where *ex aequo et bono* taxpayer is not entitled to recover.

The case of *New York & Albany Lighterage Co.* v. *Bowers*, 273 U. S. 346, 6 A. F. T. R. 6541 is alone sufficient to show that an action on income taxes is an action to enforce a statutory right and is not equitable in nature. In that case, even before Section 607 of the 1928 Act or any similar provision was passed, this Court held that a suit against the Collector, identical with the present suit, would lie to recover amounts collected after the statute of limitations had run, where there was no other reason for recovery than that

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[1] "If the tax was erroneous and illegal, as is alleged, it must be conceded that, under the system then in force, there accrued to the taxpayer when he paid the tax a right to have it refunded without any showing as to whether he bore the burden of the tax or shifted it to the purchasers. And it must be conceded also that section 424 applies to rights accrued theretofore and still subsisting, but not sued on prior to April 30, 1928, and subjects them to the restriction that the taxpayer (a) must show that he alone has borne the burden of the tax, or (b) if he has shifted the burden to the purchasers, must give a bond promptly to use the refunded sum in reimbursing them. But it cannot be conceded that in imposing this restriction the section strikes down prior rights, or does more than to require that it be shown or made certain that the money when refunded will go to the one who has borne the burden of the illegal tax, and therefore is entitled in justice and good conscience to such relief. This plainly is but another way of providing that the money shall go to the one who has been the actual sufferer and therefore is the real party in interest." *United States* v. *Jefferson Elec. Mfg. Co.*, 291 U. S. 401-402.

the statute had run when the amounts were collected. If the suit to recover these amounts is limited by the usual limitations upon an action for money had and received, how could it possibly be availed of to recover in such a case? The English case of *Moses* v. *McFerlan,* 2 Burroughs, 1005, in which the opinion was written by Lord Mansfield, expressly says that that action will not lie to recover back a "payment of a debt barred by the statute of limitations."[2]

The opinion of this Court in *Stone* v. *White,* 301 U. S. 532, entirely ignores the inconsistency between its holding there and its decisions in the *New York & Albany Lighterage* case and the *Bull* case and adopts without qualification the view that the action is wholly equitable in nature, saying:

> "Its use to recover upon rights equitable in nature to avoid unjust enrichment by the defendant at the expense of the plaintiff, and its control in every case by equitable principles, established by Lord Mansfield in Moses *v.* MacFerlan, 2 Burr. 1005 (K. B. 1750), have long been recognized in this Court. * * * It is an appropriate remedy for the recovery of taxes erroneously collected, Elliott *v.* Swartwout, 10 Pet. 137, 156; Cary

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[2] "If the defendant be under an obligation from the ties of natural justice to refund, the law imposes a debt and gives an action founded on the equity of plaintiff's case, as it were, upon a contract quasi ex contractu, as the Roman law expresses it. This kind of equitable action to recover back money which ought not in justice to have been paid is very beneficial and therefore much encouraged. It lies only for money which ex aequo et bono the defendant ought to refund. It does not lie for money paid by plaintiff which is claimed of him as payable on a point of honor or honesty although it could not have been recovered from him through any course of law, *as in the payment of a debt barred by the statute of limitations,* or contracted during infancy, or to the extent of principal and legal interest upon a usurious contract, or for money lost at play, because in all these cases the defendant may defend with a safe conscience, though by positive law he is barred from recovery. In other words, the gist of this kind of action is that the defendant, under the circumstances of the case, is obliged by the ties of natural justice and equity to refund the money." *Moses* v. *McFerlan,* 2 Burroughs, 1005. (Italics supplied.)

> *v.* Curtis, 3 How. 236, 246-250. The statutes authorizing tax refunds and suits for their recovery are predicated upon the same equitable principles that underlie an action in assumpsit for money had and received. United States *v.* Jefferson Electric Mfg. Co., 291 U. S. 386, 402. Since, in this type of action, the plaintiff must recover by virtue of a right measured by equitable standards, it follows that it is open to the defendant to show any state of facts which, according to those standards, would deny the right."

And the very first case cited by the Court is the English case of *Moses* v. *McFerlan,* above referred to[3] which is directly inconsistent with the heretofore unquestioned holding of this Court in the case of *New York & Albany Lighterage Co.*

It is respectfully submitted that when consideration is given to all the pronouncements of this Court on the subject of the nature of an action to recover taxes overpaid, and to the cases where the action is admittedly available to recover money which was owed by the taxpayer and which he is not *ex aequo et bono* entitled to have refunded, as in cases where the sole ground of recovery is that the tax was paid after the statute of limitations had run, this Court will not adhere to any view that an action for the recovery of taxes is an action equitable in nature dependent upon a showing that the Government has money to which, in justice and equity, plaintiff is entitled. On the contrary this Court must hold that the action is legal in nature and dependent only upon a showing that the taxes sued for have been overpaid.

That does not mean that an action to recover taxes overpaid is not, like all other legal actions, subject to certain

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[3] This case is also cited and quoted from by the Court below in the present case in support of its holding that the action is one for money had and received. (R. 61.)

equitable defenses, but it does mean that an action to recover back taxes is subject only to such defenses as would at the time the taxes were collected have permitted the Government to prevail in an action against the taxpayer. If the taxpayer has acted in such a way in some other taxable period as to deprive himself of the right to insist that his taxes for the taxable period in question be computed on what would under the statute alone be the correct basis—as where he has misrepresented a fact in an earlier year to the detriment of the Government and is in the later year held bound by that misrepresentation—he might be denied a refund to which, under the strict provisions of the statute alone, he would be entitled. But recovery would be denied, not upon the ground that the action to recover taxes is equitable or that a taxpayer is not definitely entitled to recover an admitted overpayment of taxes without regard to equities, but upon the ground that, under the facts which he has a right to present, no *overpayment* is shown to have occurred.

A holding that, where there has occurred an admitted overpayment of taxes which the Government could not legally have collected, such overpayment may not be recovered back because of some theory of inequity, would lead to most deplorable results. It would be most unfortunate if an officer, clothed with the vast power of summary action which rests with the Commissioner of Internal Revenue, could, by collection of amounts not due or barred by the statute of limitations, place himself in a better position to *keep* such money than he would have been in to *collect* it, had he been compelled to sue. Such a holding would invite lawlessness on the part of officials.

To permit the Government under such circumstances to retain illegal collections would necessitate the wide spread use of injunctions against the collection of taxes. The tax-

payer, in order to secure the injunction, could show facts which, after the tax is collected, might provide for the Government in a suit for refund the defense that the taxpayer *ex aequo et bono* is not entitled to recover. It is not difficult to picture the costly confusion into which the tax collecting agencies of the Government would be thrown by this extensive use of the injunction. Nevertheless, it is even more difficult to conceive of this Court's refusing an injunction where a real danger existed that an illegal tax once collected might successfully be withheld.

It is believed that this Court can search in vain through the revenue statutes for any suggestion that Congress has ever contemplated any such holding except under certain special circumstances expressly provided for by Congress.[4] Congress has generally shown a very wise desire to have taxpayers feel that they can make prompt payment of any taxes claimed from them, or which upon their own computation they feel they may owe, with the full assurance that if the taxes have been overpaid, that is, if the amounts paid are not such as the Commissioner could have legally collected for the year for which paid, the amounts so overpaid will be refunded or credited against unbarred liabilities which are collectible against the taxpayer. Congress has been careful to see to it that a taxpayer generally is not discriminated against in any way because he may actually have paid over his money or because of the manner in which the overpayment occurred.

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[4] Section 611 of the Revenue Act of 1928 (*Graham* v. *Goodcell*, 282 U. S. 409); Section 424 of the Revenue Act of 1928 (*Jefferson Electric Company* v. *United States*, 291 U. S. 386); Title VII of the Revenue Act of 1936 (*Anniston Manufacturing Company* v. *Davis*, 301 U. S. —). In the opinion of the writer it is unfortunate that Congress has seen fit in these few exceptional cases to depart from the general rule that a taxpayer is not prejudiced in any way by having paid a tax alleged to be due. It would be unfortunate in the extreme to have the Court hold that persons out of these special classes should be prejudiced by payment.

Sections 607 and 609 of the Revenue Act of 1928[5] require absolutely that amounts collected by *payment or credit* after the statute has run *shall constitute an overpayment* and expressly direct that *"it shall be refunded"*, provided only that a claim for refund is filed within time. Congress had already provided in 1924 that suit for refund could be maintained to recover a tax overpaid, although the payment was not made under protest. Congress has thus attempted in every way to see that a taxpayer is not deprived of the benefit even of the statute of limitations because the Government may wrongfully collect or he may ignorantly pay a barred tax, without any regard whatever to whether *ex aequo et bono* the tax was owed. Certainly there is no reason for this Court sanctioning any departure from the sound policy laid down by Congress even if it properly had authority to do so.

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[5] Section 607 of the Revenue Act of 1928 expressly provides that any tax paid after the statute of limitations has run constitutes an overpayment, and says that "it shall be refunded", provided only that a claim is filed within time. Section 609(a) of the Revenue Act of 1928 provides that if the Commissioner credits any amount against a barred liability, such credit shall be deemed an overpayment under Section 607. These are positive provisions of law expressly directing refunds not only of amounts paid by or collected from the taxpayer on assessments barred by the statute of limitations, but going further and expressly commanding by statute that there be refunded to taxpayer any amounts of any overpayments made by the Taxpayer which the Commissioner has credited against a barred liability. Certainly, the Courts should not require or permit the doing of what Congress has expressly prohibited.

Section 322 of the Revenue Act of 1928 provides that where a taxpayer has paid more than he owes for any year, the amount shall be credited against other taxes due by the taxpayer, and the balance "shall be refunded immediately to the taxpayer." When this is read in connection with Sections 607 and 609(a), it is clear that if the only outstanding liability is barred by the statute of limitations, refund is expressly commanded by statute.

And certainly it would be anomalous to defeat the very express commands of these statutes by holding that refunds cannot be secured if other amounts of tax are outstanding and barred, because under such circumstances the defendant does not have money to which *ex aequo et bono* plaintiff is entitled.

The Committee on Federal Taxation of the American Bar Association, has this year in its report pointed out the necessity of preserving the feeling on the part of taxpayers that the system is fairly administered and has called attention especially to the undesirability of having a different rule prevail in suits by a taxpayer to recover a tax overpaid from that which would prevail in a suit by the Government to collect the tax if it had not been paid. The report of the Committee states:

> "In a taxing system such as ours in which the continuous flow of revenue depends mainly on voluntary reports and voluntary payments by taxpayers, it is highly important to the Government that taxpayers who overpay their taxes shall promptly and easily receive refunds of any excess mistakenly collected from them. If, owing to the text of the law, or to court constructions of it or to policies pursued in administration of it, an advantage accrues to the taxpayer who puts off payment as long as he can, the working of the system will be impaired because taxpayers will realize that the system penalizes them for prompt and generous disclosure and payment. From time to time all three branches of government—the legislative, executive and judicial—have occasionally shown a tendency to proceed on narrower principles, that 'possession is nine points of the law,' and that when a taxpayer is allowed a refund of an overpayment by him, it is a mere favor to the taxpayer at the Government's expense. The fact is, that the Government revenues gain immensely whenever taxpayers can say to themselves with conviction, If my Government collects too much tax from me, it will be prompt and honest in giving me the money back, with full interest."

In another portion of its report the same Committee comments on the unfavorable aspects, from the viewpoint of public policy, of courts adopting the theory that tax actions

are equitable, rather than legal, in character and of attempting to do "rough justice" in particular cases.[6]

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[6] "While there are impressive arguments in favor of courts' seeking to 'do justice' in particular cases, so far as is possible without violating the letter of the statute, it is beginning to be clear that if courts go too far into the legislative field in adjudicating tax cases, the public interest will be injured by gradually driving more and more tax cases into the courts. The more lawsuits a taxation system produces, the worse for the Government and its revenues; administrative processes are in general better adapted to revenue collection. Uncertainty as to the final outcome produces lawsuits, and uncertainty is produced whenever the outcome of a case is made to depend on the rough justice of that particular case. Taxation legislation is peculiar, in that it contemplates as a normal thing a vast number of transactions between the Government and its citizens, and those transactions cannot proceed in an orderly administrative way unless the final result is reasonably predictable.

In older court opinions over a long period, statements are frequently found that if a statute is inequitable either to the taxpayer or to the Government, the remedy lies with Congress. This position was in part predicated on the consideration that for many years it has been the practice of Congress to give frequent attention to revenue laws, amending them when they needed it—the theory being that when a doctor is present, there is little reason for a layman to prescribe. In later years, however, the courts have occasionally shown a somewhat different tendency—to go beyond the mere 'interstices' and to soften or stiffen the law by interpretation according to their views of the case before them. This tendency has, perhaps, been more observable when the so-called 'equities' were urged in favor of the Government. Even when the Government succeeds in urging such an equitable construction, the ultimate result may be against the Government's interest, because in subsequent cases, where the positions of the Government and the contending taxpayers are reversed, the result is to confuse a statute which need not have been confused.

Tendencies to apply a rather one-sided equitable construction are, perhaps, being checked even now, as may be indicated by the more careful position taken by the courts in very recent decisions in cases where the Government sought to estop a taxpayer from relying on the true facts.

It is the view of the Committee that the substantial number of tax cases pending in courts at this time is in part due to the unpredictability as to the result in many problems affecting the revenue and that this situation is fostered in part by 'rough justice' in court decisions." Report of the Standing Committee on Federal Taxation, American Bar Association Meeting, September, 1937.

Conclusion.

For the reasons stated, this Court, in disposing of this case, should remove all doubt from the long-established rule that court actions involving taxing statutes are legal actions which should not be disposed of on equitable grounds.

Respectfully submitted,

ROBERT ASH,
Munsey Building,
Washington, D. C.,
Amicus Curiæ.

October 12, 1937.

SUPREME COURT OF THE UNITED STATES.

No. 6.—October Term, 1937.

D. W. McEachern, Administrator of the Estate of S. C. McEachern, Deceased, Petitioner,
vs.
J. T. Rose, Former Collector of Internal Revenue for the District of Georgia.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit.

[November 8, 1937.]

Mr. Justice Stone delivered the opinion of the Court.

This petition for certiorari raises the question whether overpayments of income taxes for the calendar years 1929, 1930 and 1931 are so related to a tax on income which should have been but was not assessed against the taxpayer for the year 1928, as to preclude recovery of the overpayments although collection of the 1928 tax is barred by the statute of limitations.

In 1924 petitioner's decedent sold five hundred shares of the corporate stock of an insurance company for the sum of $300,000, at a net profit of $295,000 over 1918 cost. Ten per cent. of the purchase price was paid at the time of sale and the balance was to be paid in installments, aggregating annually 10% of the purchase price, in each of the nine succeeding years. As permitted by the applicable statutes (§ 202, Revenue Act of 1924, c. 234, 43 Stat. 255; §§ 202, 212, Revenue Act of 1926, c. 27, 44 Stat. 11, 23; § 44, Revenue Act of 1928, c. 852, 45 Stat. 805), decedent elected to return the profit for income taxation on the installment basis. After his death in 1928 petitioner, as his administrator, filed income tax returns in behalf of his estate for the calendar years 1928 to 1931 inclusive, showing in each year a sale of fifty shares of the stock of the insurance company at a net profit of $29,500. These returns were erroneous in point of fact and of law, as the petitioner sold no shares of the stock in any of those years and since, by reason of the

provisions of § 44 (d) of the 1928 Act[1] the capital gain included in the value of the unpaid installments at the time of decedent's death, was income taxable to decedent for the year 1928 and not in subsequent years.

By the provisions of § 44 (d), as construed by Treasury Regulations 74, Art. 355, the transmission of an installment obligation at the death of the payee capitalizes the unpaid installments of the contract and results in taxable gain to the estate of the decedent, measured by the difference between the fair market value of the obligation at the time of his death and its unrecovered cost. By § 113 of the 1928 Act the basis for computing the annual profit upon the installments paid after the decedent's death is the fair market value of the contract at the time of his death. The unpaid tax for 1928, computed as required by § 44 (d), exceeds the sum of the overpayments made in 1929, 1930 and 1931.

On the trial in the district court the collector contended that petitioner was estopped to deny that the sales of stock occurred and profit accrued as reported in his returns for the years in which refunds were claimed; and that, in any case, upon equitable principles, the petitioner was not entitled to recover the overpayments for those years, since they were less in amount than the tax which should have been assessed against him for 1928. See *Stone* v. *White*, 301 U. S. 532. The trial court overruled these contentions and gave judgment for petitioner. The Court of Appeals for the Fifth Circuit reversed, holding that petitioner was not in equity and good conscience entitled to recover the overpayments which, because of his failure to pay the 1928 tax, had resulted in no unjust enrichment of the Government. 86 F. (2d) 231. We granted certiorari, 301 U. S. —, because of the importance of the question in administration of the revenue laws.

The collector does not press here the contention that petitioner is estopped to challenge the correctness of his returns for the years

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[1] Sec. 44.

(d) *Gain or loss upon disposition of installment obligations.*—If an installment obligation is . . . distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and . . . the fair market value of the obligation at the time of such distribution, transmission, or disposition. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full.

of overpayment. The failure of the Government to assess the appropriate tax in 1928 is not shown to be attributable to the erroneous statements made in the returns for the later years, and it is not necessary for petitioner to show understatement of the income taxable in 1928 in order to show the correct amount of the different income derived from the installment contract in the years of overpayment. For, under § 113, the overpayments are established by showing that in each year the amount of income from the sale of the stock as reported exceeded the difference between the installments collected and so much of the value of the installment contract at the death as is allocable to the taxable year. But respondent insists, as the court below held, that petitioner is not equitably entitled to recover overpayments of taxes upon the profits derived from the contract in certain years because the overpayments are exceeded by a tax which he should have paid on the profits realized in an earlier year.

We may assume that, in the circumstances, equitable principles would preclude recovery in the absence of any statutory provision requiring a different result. But Congress has set limits to the extent to which courts might otherwise go in curtailing a recovery of overpayments of taxes because of the taxpayer's failure to pay other taxes which might have been but were not assessed against him. Section 607 of the 1928 Act declares that any payment of a tax after expiration of the period of limitation shall be considered an overpayment and directs that it be "credited or refunded to the taxpayer if claim therefor is filed within the period of limitation for filing such claim"; and § 609 (a) of the 1928 Act provides that "Any credit against a liability in respect of any taxable year shall be void if any payment in respect of such liability would be considered an overpayment under section 607." These provisions preclude the Government from taking any benefit from the taxpayer's overpayment by crediting it against an unpaid tax whose collection has been barred by limitation.

It is plain that these provisions forbid credit of the overpayments of taxes for 1930 and 1931, which were made after collection of the 1928 tax was barred. If petitioner had then paid the 1928 tax there would have been an overpayment of the tax, refund of which is made mandatory by § 607. Credits against the tax of overpayments of taxes assessed for other years, if made at that

time, could not stand on any different footing under the provisions of § 609. The right of the government to credit the overpayments upon the earlier unpaid tax could arise only when the overpayments occurred; but since at that time collection of the 1928 tax was barred by limitation, and payment of it would be an overpayment, credit against it of the 1930 and 1931 overpayments was forbidden by § 609.

Different considerations apply to the 1929 overpayment. When it was made, collection of the 1928 tax was not barred and the commissioner was not then prevented by § 609 from crediting the overpayment upon the 1928 tax, although he did not do so. Section 322 of the 1928 Act,[2] continued without material change in the 1932 Act, authorizes the credit of an overpayment of any tax against any income tax "then due" from the taxpayer, and directs that any "balance shall be refunded immediately to the taxpayer." We need not inquire whether the 1928 deficiency was "due" within the meaning of this section before the tax was assessed, for in any case there could be no credit against the tax of the 1929 overpayment, before the amount of the latter was ascertained and allowed and at that time collection of the 1928 tax was barred and any credit of the overpayment against it was declared to be void by § 609.

Both § 322 and § 609 contemplate that the time of credit of an overpayment in one year against a tax for another is to be marked by some definite administrative action. This Court, upon an examination of the established practice in the Bureau of Internal Revenue, concluded that the time of allowance of a refund and the time of credit of an overpayment against a tax due, is the date of approval by the commissioner of the schedule of refunds and credits prepared by the collector, showing the amount due the taxpayer, rather than the earlier date of the certification by the commissioner to the collector, of the schedule of overassessments. See *United States* v. *Swift & Company,* 282 U. S. 468; *Girard Trust Company* v. *United States,* 270 U. S. 163. We ac-

[2] Sec. 322

(a) Authorization.—Where there has been an overpayment of any tax imposed by this title, the amount of such overpayment shall be credited against any income, war-profits, or excess-profits tax or installment thereof then due from the taxpayer, and any balance shall be refunded immediately to the taxpayer. . . .

cordingly held that approval of the schedule of refunds and credits fixes the date from which interest is allowed upon any balance refunded to the taxpayer, *Girard Trust Company* v. *United States, supra,* and the date from which the statute of limitations runs against the taxpayer's right to demand refund of a tax paid by the allowance of a credit. *United States* v. *Swift & Company, supra.*

After these decisions § 1104 of the Revenue Act of 1932, c. 209, 47 Stat. 287, changed the date which should be deemed to be the time of allowance of the credit or refund within the meaning of that and earlier revenue laws. It provided that "Where the Commissioner has (before or after the enactment of this Act) signed a schedule of overassessments in respect of any internal revenue tax imposed by this Act, or any prior revenue Act, the date on which he first signed such schedule (if after May 28, 1928) shall be considered as the date of allowance of refund or credit in respect of such tax."

The date of the claim for refund and the date of the allowance of the credit which, according to § 1104, was that of the approval by the commissioner of the schedule of overassessments, came after recovery of the 1928 tax was barred. If petitioner had then paid the tax he could have recovered it back as an overpayment under § 607; accordingly, credit against the tax of the 1929 overpayment is prohibited by § 609, as are like credits for the overpayments of 1930 and 1931.

The similar treatment accorded by the statutes to credit against an overdue tax, and to payment of it; the prohibition of credit of an overpayment of one year against a barred deficiency for another; and the requirement that payment of a barred deficiency shall be refunded, are controlling evidences of the Congressional purpose by the enactment of §§ 607 and 609 to require refund to the taxpayer of an overpayment, even though he has failed to pay taxes for other periods, whenever their collection is barred by limitation.

Sections 607 and 609 do not apply in the circumstances disclosed in *Stone* v. *White, supra.* There testamentary trustees had paid from income a tax upon it which should have been paid by the beneficiary, and it was held that they were not equitably entitled to recover the tax after the statute had barred collection from the beneficiary. The assessment of a deficiency against the trustees and the payment of it by them were not barred by limitation. Hence

§ 607 did not compel a recovery. Section 609 did not require it. The commissioner neither sought, nor did § 322, regardless of any period of limitation, permit him to credit the amount which the one taxpayer had paid against the tax which another should have paid. Equitable considerations not within the reach of the statutes denied a recovery. It was enough, in the peculiar facts of the case, that the trustees had suffered no burden and that the Government was not unjustly enriched.

Reversed.